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UNITED STATES SMALL BUSINESS ADMINISTRATION
LOS ANGELES DISTRICT OFFICE

REPORTER'S TRANSCRIPT OF
PUBLIC HEARING ON SIZE STANDARDS

WEDNESDAY, JUNE 29, 2005
8:35 A.M.

330 NORTH BRAND BOULEVARD
GLENDALE, CALIFORNIA

Taken before: DANEE SHAHEEN, RPR,
CSR No. 1652

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PANELISTS:

John Klein (OGE), Office of General Counsel
Gary M. Jackson (OISS), Office of Size Standards
Nicholas Manalisay (OIG), Office of Government
Contracting

Alberto G. Alvarado, District Director

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GLENDALE, CALIFORNIA, WEDNESDAY, JUNE 29, 2005
AT 8:35 A.M.
* * *

MR. ALVARADO: Good morning. Let me ask you to
take your seats.

Thank you. Thank you so much.
Page 1

8 Good morning. I'm Alberto Alvarado, the
9 District Director of this local office of the Small
10 Business Administration. I would like to informally
11 welcome you to your SBA office for what I hope is either
12 the first of your many visits to this office or one of
13 your frequent visits to this office.

14 In either event, remember that this is, in
15 fact, your office. We like to see you here often for,
16 frankly, all your small business needs.

17 The L.A. office of the SBA has the distinction
18 of being the highest volume office of the SBA in the
19 country. Over the past couple of years, we have
20 financed 11,000 small businesses with \$2.3 billion.

21 We facilitated the award of about \$2 billion in
22 88 contracts, and we trained or counseled over 100,000
23 small business entrepreneurs. We are proud of being the
24 top financier of minority and women-owned businesses in
25 the country.

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1 More to the point today, we are also proud of
2 being at the cutting edge of small business innovation,
3 of novel initiatives, and of insightful thinking about
4 the evolution of small businesses in our country.

5 This is why we're honored to host this size
6 standard hearing and to have the pleasure of your
7 company and your patience, and to convene together for
8 the purpose of dialogue on a vital topic, a complex
9 topic, and a topic near and dear to all of us and to the
10 future of our country.

11 Now, when we contemplate such a ponderous and
12 quite possibly as intractable as the SBA's size
13 standards and the challenge of crafting fair and
14 balanced standards to support and promote the
15 advancement of America's economic engine, I'm reminded
16 of the new judge who had the occasion of being in his
17 courtroom for the first time, and he called the
18 plaintiff up on his first case, and he says, "Please
19 present your case."

20 The plaintiff lawyer finished.

21 The judge said, "You win."

22 The defense counsel said, "Well, gee, Your
23 Honor, this doesn't seem quite fair. What about us
24 being allowed to present our case?"

25 So the judge said, "Yes, yes, please present

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1 your case."

2 The defense attorney presented his case.

3 The brand new judge then said, "Ain't that
4 something? Now the defense wins."

5 Not a very funny judge. Maybe not a very funny
6 district director. Let me go back to work on that, or
7 let me try to explain it to you.

8 Really what that story illustrates -- in not a
9 very funny way apparently -- is how difficult some
10 decisions are and that sometimes it just ain't easy, as
11 the judge said. One minute the plaintiff wins; one
12 minute the defendant wins.

13 When you have such strongly persuasive
14 viewpoints, it isn't easy deliberating between those
15 views. However, we know that today our deliberations
16 will be guided by principles, by introspection, and by
17 thoughtful analysis.

18 Let me, from that lofty perch, let me move to a

19 couple of pedestrian housekeeping items. I think
20 there's water available here. There are other sundries
21 that are available on the first floor in the southwest
22 corner of the building. See Helen down there.
23 Now, before you overpartake of the water, I
24 must warn you that there are no functioning bathrooms or
25 rest rooms on this floor. I think you have already been

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1 told that repeatedly by our staff as they're dashing out
2 to the rest rooms. Rest room facilities are available
3 on the eleventh floor and the second floor.

4 Also, should you need -- another final
5 housekeeping item is we don't validate for parking. But
6 we can provide you access to capital, access to the
7 federal procurement marketplace, and access to
8 entrepreneurial training, which are the core services of
9 the SBA. So see any one of our award-winning and
10 smiling SBA staff members, of which there are a good
11 number.

12 And now it's my pleasure and also honor to
13 introduce to you for the official welcome our boss,
14 Regional Administrator Bruce Thompson. Mr. Thompson
15 oversees the SBA's number one region in the country.
16 They call him the five-billion-dollar man because just
17 this past year the offices under his authority financed
18 over 18,000 small businesses.

19 This is a man who gets it, and he knows how to
20 get it done. He knows about business because he has
21 owned four of his own businesses. He knows about public
22 policy because he has been a California state
23 legislator. He even gets it about children because he's
24 had eight.

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And he even has been able to figure out and

1 handle SBA district directors from East L.A. Imagine
2 that.

3 Ladies and gentlemen, Regional Administrator
4 Bruce Thompson.

5 MR. THOMPSON: Thank you very much.

6 On behalf of Hector Barreto, the administrator
7 of the SBA, I'd like to thank each one of you for taking
8 time out of your busy schedules to be here for this most
9 important hearing and also to thank Mr. Jackson and
10 Mr. Klein for coming from Washington to be here in
11 Los Angeles. They were in San Francisco yesterday.

12 As many of you know, this region is the largest
13 in the country, comprising California, Nevada, Arizona,
14 Hawaii, and Guam.

15 And with that, I think I'll just turn it right
16 over to you, Mr. Klein. You're going to be the
17 moderator today, and we appreciate everybody's
18 attendance. Thank you.

19 MR. KLEIN: My name is John Klein. I'm the
20 associate general counsel for the size standards of the
21 SBA. With me is Gary Jackson, who is the director of
22 the size standards staff, and Nick Manalisay, who heads
23 procurement in this area of Southern California.

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As you heard today, we'll be discussing size
standards. On March 19th, 2004, the SBA proposed a

1 complete revision to the size standard, making many of
2 them -- proposing many of them to be employee-based size
3 standards for the first time.

4 In response to that proposal, the SBA received
5 more than 4,000 comments. Many of them were not in
6 favor of that proposal.

7 In response to the comments received, the SBA
8 withdrew the proposal on July 1st, 2004, and we
9 developed an Advance Notice of Proposed Rulemaking for
10 the future.

11 Based on the comments received, the public
12 identified many issues they thought were important for
13 us to consider. And we took those comments we received
14 and put them as part of our Advance Notice Proposed
15 Rulemaking that we sent out.

16 In that advance notice, we invited comments on
17 any issues or anything else that the public considers to
18 be important in the size process. Again, those eleven
19 issues that we have identified were issues that were put
20 forth by the public. They're not SBA's views or SBA's
21 proposals at this time.

22 SBA is seeking comments on each of those issues
23 and other issues you think are important for the size
24 process. And once we have reviewed all these comments,
25 we will then go forth and make the proposal which you

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1 will have further opportunity to comment on as part of
2 the rulemaking process.

3 Today your testimony will be recorded by a
4 certified court reporter. When you get to the podium,
5 please state your name and spell it and identify the
6 firm or organization that you are with for the record,
7 please.

8 Please note the record is all in the order that
9 you signed in this morning. And then we also have a
10 list of attendees that were presented to us before for
11 registration.

12 I'll go through all those names, even the ones
13 that have not been given numbers at this point in time.
14 At the end of the day, if I call a name and they do not
15 come forth, I will try again to afford equally the
16 opportunity before the morning session ends.

17 Each individual will be allowed five minutes
18 for their whole presentation. I will advise you when
19 the time is up, but there will also be a timer here in
20 the front row who will identify the one-minute mark and
21 when the time is up so that everyone knows where they
22 are in the process.

23 Obviously, we're not going to cut you off at
24 five minutes exactly. If you'd finish up your thought,
25 that's fine. There's no problem with that.

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1 If you have any written testimony that you want
2 to present to us, that's fine. Do it before or after
3 your presentation. We'll take it back with us to
4 Washington.

5 Members of the panel may ask you questions
6 during your testimony or within your testimony, and that
7 will constitute your five minutes.

8 The panel will not respond as to whether it
9 agrees or disagrees with the position being presented.
10 We just ask for clarification of your position, of what
11 you think. We're really here to understand what the
12 positions are. We are again in the formulating stages,
13 and we want to know exactly why you think what you think
14 and what specifically you think.

15 A discussion of issues unrelated to size
16 standards will not be appropriate and will be stopped.

17 Members of the press are asked to identify
18 themselves and sign in on a separate sheet in the back.
19 I'm sure that has already been taken care of.

20 So with that, let's get started. The first
21 person is Larry Flood.

22 MR. FLOOD: Good morning. My name is Larry
23 Flood. My wife and I -- Lois -- we own a company called
24 Express Personnel Services of Rancho Cucamonga -- and,
25 yes, it is a city in Southern California.

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1 Obviously, she is a minority owner. I'm a
2 veterinarian -- veteran, and I come from a background of
3 middle management and upper management with a Fortune
4 200 company. I was downsized from that.

5 I went out to seek further opportunities. We
6 decided on staffing as a business after exploring lots
7 of other options. And through that, then we went out to
8 find companies and funding sources and places that we
9 could go to accomplish opening a staffing company.

10 After a lot of research, we found a company
11 called Express Services that offered a bundle of
12 services, and we decided that that would be the best way
13 for us to go. So we signed up with them.

14 We then went out and leased a spot. Our lease
15 is under our name, not under our franchisor's name. We
16 obtained insurance. We obtained business permits and
17 all other aspects -- furniture, computers, and
18 everything goes with that -- under our name. We are
19 solely responsible for the financial responsibility for
20 those purchases and services that we have obtained.

21 We picked out the area. We designed our
22 offices. They are our design and our vendors that we
23 purchase.

24 If we fail to meet any of the stipulated
25 agreements through our lease or through our other

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1 financial arrangements with other companies, banks, and
2 lending institutions, there's no recourse to our
3 franchisor.

4 My house is on the line. We have to pay for
5 the burden of that. We chose Express Personnel. We
6 bought and purchased their systems. That would allow us
7 to get a little bit further down the line with our
8 growth.

9 We are responsible for hiring, recruiting,
10 training, evaluating, drug testing, and all other
11 aspects of the people that come into our doors. Our
12 franchisor does not do any co-op advertising, nor do
13 they do any advertising on our behalf. We pay for all
14 of that 100 percent. We design and do that all on our
15 own.

16 We have an internal staff of four people,
17 including my wife and I, and that process is all
18 outsourced to another company. So we've outsourced that
19 to a company up in Oregon.

20 We outsource a number of other business
21 aspects. We have an accountant that does our work for
22 us. We have a lawyer that's responsible for helping us
23 and keeping us out of trouble.

24 The business decisions and the day-by-day
25 operation of our offices are totally Express of Rancho

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1 Cucamonga. The franchisor does not get into that side
2 of it. They handle the payroll for us. They do the
3 reporting, and they do the taxes, withholding for us.
4 And that's what we bought and that was part of the
5 package. We also bought their software package.

6 Without their services, if they didn't exist,
7 we would still exist as a company. We would go outside,
8 buy the bundled packages. Or independently we would buy
9 funding, we would buy payroll, we would buy computer
10 systems, of which there are plenty, to do all those
11 functions for us.

12 The franchisor has no responsibility for us and
13 our decisions to do business with companies. And some
14 of those -- most of those times are good; some of them
15 are not.

16 We got stuck some years ago with
17 Montgomery Ward when they went out of business. We had
18 \$7,800 in cost there that we couldn't recuperate that
19 was part of their going out of business.

20 We had another company the following year,
21 Omega Warehousing, costing us approximately \$31,000 in
22 revenues as well as \$9,000 more in legal fees, of which
23 we bore the entire 100 percent of that.

24 We had a contracting company that worked out at
25 Frito Lay the following year that cost us \$17,000. That

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1 was a write-off for our offices and has nothing to do
2 with the franchisor.

3 So pretty much in summary, our business is a
4 California corporation. We are separate and distinct
5 from our franchisor. All the day-to-day business
6 decisions are ours to make. We have the opportunity to
7 fail or succeed, as we may be.

8 The franchisor has no vested interest in that.
9 So we move forward, knowing that. We have been in
10 business almost ten years. No, it's not been fun the
11 first few years, but now it is. And we've done well.
12 We've come a long way.

13 And so now our success is because of what we
14 have done, our office staff has done, and my wife and I
15 personally have done. We bought a franchise to get
16 services from them. Okay.

17 Thank you very much.

18 MR. KLEIN: A few questions.

19 Under SBA rules, franchisees may be eligible
20 for professional businesses depending on the franchise
21 agreement. I know with the Express Personnel case, for
22 instance, we have some concerns overriding regarding the
23 franchise agreement itself and whether there was too
24 much control by the franchisor.

25 For instance, you were talking about when firms

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1 went out of business, you bore the brunt of the entire
2 amount of what they owed?

3 MR. FLOOD: That's right.

4 MR. KLEIN: Now, what happens with the
5 franchisor? Did you have to pay them in that situation
6 for their portion of the --

7 MR. FLOOD: They received 100 percent of the
8 fees that were due to them. I received nothing from the
9 business that I did. I paid the payroll taxes and the
10 unemployment, the franchise fees, and all the other

11 costs were incurred 100 percent by our business.

12 MR. JACKSON: It's my understanding that in the
13 Express Personnel franchise agreement, the franchisor is
14 the employer of record. And you had mentioned you hire,
15 fire, train, and place, and you recruit.

16 Does the franchisor have any direct
17 responsibility with respect to those employees in terms
18 of placement, in particular, or for particular clients
19 or in any related way, or is that totally under your
20 control?

21 MR. FLOOD: All aspects of that are under our
22 control. We interview the people. We recruit the
23 people. We train them, screen them all at our cost.
24 And we go out and solicit businesses, and we choose to
25 do business with whoever we want to do business with.

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1 Our franchisor takes care of the reporting and
2 the payroll functions. Invoicing goes out by them,
3 incomes are received by them, and we get in return our
4 money for that.

5 And so, no, we have 100 percent responsibility
6 for our associates.

7 MR. KLEIN: If, in theory, the franchisee went
8 into bad financial straits and went out of business, as
9 the employees are the employees of the franchisor, would
10 they be assigned to other franchisees at that point in
11 time, or what would happen?

12 MR. FLOOD: I'm not sure, but we don't have one
13 that's close by us. So I don't know if it's even a
14 viable alternative. And so I don't know how that would
15 be handled.

16 Obviously, we've got people that are working
17 and being paid. They aren't just going to be abandoned
18 COUGH, "we're done. We're out of here." There must be
19 some -- and I don't know what it would be from that --

20 MR. KLEIN: But the payroll -- I'm sorry; not
21 the payroll -- the way the payment is made directly to
22 the franchisor, it appears to us as commission that you
23 are getting paid as opposed to your particular shares.
24 It looks like you're taking a share as opposed to their
25 taking a share, if that makes sense.

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1 Can you follow up on that.

2 MR. FLOOD: Yeah, they do the accounts
3 receivable for us. They manage that piece. We can
4 choose to go outside and find somebody else that will do
5 that. There are plenty of companies that will do that
6 for us. We receive --

7 MR. KLEIN: Do you have a choice to do that
8 with them or not?

9 MR. FLOOD: When we bought the bundling, no.
10 We chose on purpose to buy complete bundling, one-stop
11 shopping. Is it available to us? Absolutely. I can go
12 out there and we can get funding and all of the other
13 pieces that they offer to us.

14 As far as taxes and withholding, they do all of
15 that for us, and they pay all of that to the various
16 organizations that take withholding out of paychecks.

17 MR. KLEIN: Thank you.

18 MR. FLOOD: Thank you.

19 MR. KLEIN: Richard Lopez.

20 MR. LOPEZ: My name is Richard Lopez. I'm a
21 certified public accountant with an office here in

22 Pasadena. I'm also an 8(a) certified firm. I received
23 my 8(a) certification last May. I have four special
24 staff.

25 And I'd like to thank you for the opportunity

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1 to be here. I want to also commend Alberto and his
2 staff here in the Los Angeles office. I think they do a
3 great job here. They've got some great people and great
4 resources.

5 I'm also a vice chairman of the SBA National
6 Advisory Council. And to repeat the SBA's mission or
7 part of the mission, it's to strengthen the American
8 economy via small business.

9 Small business -- you know, a big chunk of my
10 client base is small to medium-sized businesses, ranging
11 anywhere from a couple hundred thousand in revenue to
12 probably no more than -- well, my largest client is
13 about 20 million in revenue.

14 The majority of them have far less than 500
15 employees. I would say that the majority of my client
16 base are probably in the 5 to 50 employee range.

17 Having said that, you know, that little segment
18 of my own client base represents one of the largest
19 sections of the U.S. economy.

20 So in the advance notice, the SBA proposed
21 several things, I think all of which impact directly on
22 small businesses. They want to simplify the size
23 standard. Right now we have nine industry groups. I
24 think that's probably plenty.

25 And the last thing SBA wants to do is make the

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1 regulations so complex that they start matching the IRS
2 code. I mean, seriously. It's not a joke because a lot
3 of people have problems with the current size standards,
4 but for the most part, they're fairly easy to read.

5 In terms of calculating the number of employees
6 for size standards, it seems to me, again, that for the
7 most part, 500 seems to be -- for most industries, that
8 is the low end of the number. Some industries are
9 higher, but 500 is the lowest.

10 Again, for most small businesses in the
11 United States and from my client base, they're not even
12 close to 500. So increasing -- any sense of increasing
13 that, I think, would be counterproductive to small
14 business.

15 In the area of using receipts-based standards
16 and in terms of -- I think receipts-based standards
17 along with revenue size requirements, I think those
18 standards as stated right now are fairly adequate.

19 In my own industry, which has a size standard
20 of 7 million, a firm -- for a special services firm such
21 as mine or a law firm, the size of 7 million
22 represents -- it means I'd probably have roughly 40 to
23 50 employees, still not a large firm, but large enough
24 to probably compete with a lot of the major firms in
25 certain markets.

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1 I think that for purposes of small business
2 set-asides, those revenue standards really do not have
3 to be increased.

4 The one area that I would suggest possible
5 changes does pertain to revenue size in that the size
6 standards may be modified such that small business

7 set-aside business is accounted for separately from
8 non-set-aside business, the example being that if, in
9 the case of my firm or a small business -- say, a
10 business doing roughly a million dollars a year in
11 revenue.

12 As an 8(a) firm or a small business, I go out
13 and bid, I get successful, and I'm able to get that
14 6-million-dollar contract, but it happens to be a
15 one-year contract. Let's say it's a small business, a
16 small business contract.

17 That one year I'm over the limit. I lose my
18 8(a) status. I'm no longer considered a small business.
19 It's great that I have the -- after one year, it's
20 not -- it's a one-year contract, it's gone. I'm back to
21 that small size again, but I can't reapply for 8(a).

22 So I would think that you could do one of two
23 things: One is do a three to five-year income averaging
24 or looking at non-set-aside business as the standard.

25 To conclude, I'm opposed to any tiered size

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1 standards. I'm against grandfathering. I'm against any
2 exclusions for venture capital firms, and I'm against
3 any changes for franchisees.

4 I want to thank you for the opportunity to
5 speak

6 MR. JACKSON: Thank you.

7 I have just one question. When you say not to
8 count revenue from a set-aside contract, is that
9 something that could be easily identified in your
10 accounting system --

11 MR. LOPEZ: Absolutely.

12 MR. JACKSON: -- or would that be difficult to
13 verify?

14 MR. LOPEZ: For a set-aside business -- I mean,
15 for anybody who's doing work for the government, you
16 basically have to have some kind of project-driven
17 accounting system. So it should be very simple to
18 report that separately.

19 MR. ALVARADO: Richard, just to be clear.
20 Again, in your instance in your industry, a
21 6-million-dollar size standard, you would aggregate your
22 small business set-aside and your 8(a) work separately.
23 The only thing that would count toward the 6 million
24 would be a nonspecified small business?

25 MR. LOPEZ: Correct. No, no. Right now I'm an

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1 8(a). I have no federal contracts right now. I'm going
2 after them, but I'm not -- and I'm roughly a million
3 dollars in revenue. Okay.

4 If, say, I got real lucky, got real successful,
5 because I go to Washington quite often right now to try
6 to launch new business. Say I picked up two
7 3-million-dollar contracts next week, but they were
8 one-year contracts. All of a sudden I go to 7 million.
9 I lose my 8(a) status; right?

10 MR. ALVARADO: Well, it is in the average
11 annual receipts over the three years standard. But
12 let's say you got a 9-million-dollar contract.

13 MR. LOPEZ: Okay. 9 million. You know, I lose
14 my small business designation, and it's a short-term
15 contract. Say, it's a project-driven work. It's doing
16 some Sarbanes-Oxley work for one of the federal
17 agencies. You know it's coming in. It's not going to

18 be continuous. Okay.

19 So I do that work. I lose -- I mean I run the
20 potential of losing my 8(a) status, losing any of the
21 ability to get set-aside business. For that two,
22 three-year period, I'm living large. Things are great.
23 Okay.

24 But then it's done, and I go back -- and I have
25 to -- and I'm going back to my essentially core business

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1 that I had before. I can't go back to 8(a). Okay. I
2 guess I can still go after small business. I can go out
3 and get classified as small business. But that, you
4 know, takes -- you know, I'm up -- for a period of time,
5 I'm out of the market for the ability to get that small
6 business work.

7 So that's why I think that income averaging or
8 a separate calculation for non-set-aside business would
9 be more appropriate. The point being is that the small
10 business set-aside work is there to promote small
11 business, to help gain them infrastructure.

12 MR. KLEIN: Thank you.

13 MR. LOPEZ: Thank you.

14 MR. KLEIN: Joey Quinto.

15 MR. QUINTO: Good morning, everyone. My name
16 is Joey Quinto. For the record, it's spelled J-o-e-y,
17 Q-u-i-n-t-o. I'm the publisher of "California Journal
18 for Filipino Americans." I'm an 8(a) contractor and
19 also a small business advocate. I'm proud to be in the
20 best district for the U.S. SBA and proud and grateful to
21 have Alberto Alvarado as the district director.

22 MR. ALVARADO: Now, listen to this man.

23 MR. QUINTO: I firmly oppose the proposal of
24 the U.S. Small Business Administration to change the
25 size standard.

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1 To the Honorable Hector Barreto, the SBA
2 Administrator, you are a former small business owner.
3 I'm confident that you totally understand the issues of
4 small businesses.

5 We in the small business community look up to
6 Mr. Barreto as the advocate of all the advocates who
7 fight for small businesses.

8 Mr. Barreto, please take the leadership not to
9 change the size standard. In the past there were 6,000
10 8(a) participants. Only 25 percent got contracts.
11 Those include 8(a) contractors that received less than
12 \$20,000 in contracts.

13 Now, there are 9,000 8(a) contractors. Lesser
14 percentage get contracts. Therefore, before adding more
15 contractors to avail small business contracts, federal
16 contracts, take care of the existing small businesses
17 first.

18 I hope that the United States Small Business
19 Administration will fight to level the playing field.
20 At the present time, the small businesses are having a
21 tough time getting federal contracts from the
22 government.

23 What would happen if the bigger companies
24 become small businesses by the definition of the SBA?
25 Let us keep in mind that small businesses currently

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1 employ more than 50 percent of the work force in the
2 United States of America.

3 If SBA allows bigger businesses to become small
4 businesses by definition, several small businesses would
5 not be able to compete and would be forced to lay off
6 employees.

7 Ultimately, many small businesses would be
8 forced to shut down their businesses. As a result, the
9 United States of America would have the highest record
10 of unemployment. Are we prepared to face this kind of
11 challenge? Not at all.

12 We would be grateful if SBA would continue to
13 let the small businesses be the largest employers in the
14 U.S. help the small businesses grow so that someday we
15 can become large businesses.

16 Let small businesses continue to become the
17 major economic engine in this country since we
18 contribute more than 50 percent of the gross domestic
19 product.

20 Let me remind you that the United States
21 Congress has formed the U.S. SBA as a federal agency to
22 assist small businesses, not the big businesses. Also,
23 the big businesses have enough resources to procure any
24 type of contracts. So don't allow them to take the
25 share of the small businesses. Otherwise, we could call

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1 this corporate greed.

2 Most importantly, don't permit the big
3 businesses to bully the small businesses. SBA, we stood
4 side by side when we fought in the same battle on the
5 issues of fighting for the small businesses.

6 The small business issue is not a Republican
7 nor a Democrat issue. It is an American issue. SBA,
8 please don't let us down. Thank you.

9 MR. KLEIN: What industry are you in?

10 MR. QUINTO: Advertising.

11 MR. KLEIN: And do you feel that the current
12 size standard is sufficient for that industry?

13 MR. QUINTO: Especially in our industry, there
14 are -- when you say giants, they are real giants. And
15 it would be very hard for a business like us to compete
16 with the giants out there.

17 MR. KLEIN: So the current standard is
18 sufficient for you.

19 MR. QUINTO: Yes.

20 MR. KLEIN: And do you prefer receipts-based or
21 employee-based size standards for that industry?

22 MR. QUINTO: Our point is I hope you would not
23 change the ruling in the middle of the game. Let's stay
24 on what we have right now.

25 MR. KLEIN: Thank you.

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1 Duane Trombly.

2 MR. TROMBLY: Good morning. For the record, my
3 name is Duane Trombly. I'm the president of a company
4 called EdgiTech in San Diego. We're a professional
5 services firm.

6 MR. KLEIN: Spell your last name.

7 MR. TROMBLY: Trombly, T-r-o-m-b-l-y.

8 I personally have been over 30 years in the
9 personal services industry both in the public and
10 private sector. I come here today as a small business
11 owner myself who works out of San Diego with small
12 corporations. We help position themselves for sale.

13 I would like to thank the panel for providing

me the opportunity to testify this morning.

The Small Business Administration was born from legislation enacted by Congress over five decades ago. In that legislation, Congress expressed a conviction that the federal government should -- and I paraphrase -- aid, counsel, assist, and protect the interest of small business concerns.

To ensure compliance, Congress set well-known, government-wide procurement standards for participation by small businesses at 23 percent of the total value of all prime contract awards for each fiscal year.

The SBA's Office of the Inspector General

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issued report No. 5-14 in February of this year, which was the result of its evaluation of the agency's compliance with its own procurement standards vis-a-vis small businesses in America.

Upon reviewing this report, it's befuddling to me as a small business owner why the very agency established by an act of Congress in 1953 to promote and protect the interests of small businesses in America would preside over the dismantling of the core of what defines a small business.

The OIG's report provides a road map to the agency's, at best, benign neglect. The agency's recommendation to reset size standards for small businesses from 100 to 1,000 to 1,500 is further befuddling in the face of the U.S. Census Bureau's oft-cited report that American businesses with less than 100 employees represent a remarkable 98 percent of all employers in this country.

For all the good this agency does for the interests of small business in America, you negate this by failing to enforce your own size standards.

The Small Business Administration's proposed rule change to simplify and restructure its small business size standards, published in March of 2004, was met with strong opposition that resulted in this very

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series of hearings across the country.

According to the OIG's report, the lack of enforcement of the established size standards has been adrift for nearly three decades across three different administrations. Grandfathering these size standards to reflect the current reality as to what companies have been receiving the small business set-asides is an attempt on the part of the SBA to codify this drift.

This cannot stand. Small businesses have been the backbone of this country since its founding. We employ more citizens and create more wealth for Americans than all the "beltway bandits" combined.

Further, for these same corporations to request five years to transition out of a small business set-aside to which they weren't entitled in the first place is cynical at best. All one needs to do, as in Watergate, is to "follow the money."

Every aspect of the proposed changes, including grandfathering, tiered size standards, venture capitalist exclusions, and affiliation regulations benefit large businesses at the expense of legitimate small businesses.

To have the agency charged with the protection of small businesses' interest in America promulgate rule

25 changes of this magnitude flies in the face of its core
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1 values. The March 2004 rules change proposal was the
2 catalyst for the SBA's own OIG to issue its finding of
3 noncompliance.

4 Yet in May of this year, the agency issued a
5 notice of public hearing on the very issue that the OIG
6 found wanting -- compliance on size standards. There is
7 an obvious disconnect within the agency on its
8 responsibility to its constituents, small businesses.
9 These kinds of behaviors further create a cynical view
10 by Americans of federal bureaucracies run amok.

11 I strongly urge the agency to roll back its
12 size standards to 100 employees for nonmanufacturing
13 companies and to use the OIG report as an instrument of
14 self-examination.

15 I'm strongly opposed to tiered standards,
16 grandfathering, and venture capitalist exclusions.

17 In closing, I want to thank the Small Business
18 Administration for the opportunity to speak out this
19 morning. I would also like to thank the American Small
20 Business League for bringing this to my attention.

21 MR. KLEIN: All right. I understand that you
22 don't like the proposal. But what would you recommend
23 as a change? Anything?

24 MR. TROMBLY: Implement the original proposed
25 size standards as they were assigned, 100 employees and
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1 the receipt issue, as they were established a number of
2 years ago. The OIG's report, Mr. Klein, tells you that
3 you have not been in compliance.

4 MR. KLEIN: In compliance with what?

5 MR. TROMBLY: The size standards. I personally
6 have knowledge that in San Diego we have small business
7 set-asides, that we have a "beltway bandit" running
8 those. It's not going to take a great deal of evidence
9 and searching to find that those violations have
10 occurred.

11 MR. KLEIN: I'm not quite sure what you're
12 speaking of, but the OIG report of which you speak did
13 not say anything about large businesses getting
14 contracts. So if that's what you're saying, that's
15 incorrect -- what you're saying.

16 What the report said was that firms that have
17 grown to be other than small over time and that continue
18 to be counted as a small business with set-asides as
19 their, if that's the problem which you speak of, we
20 should correct that problem. I don't think that's a
21 fair comment. It's not a fair comment to say that large
22 businesses are getting counted as small. I don't think
23 anyone has said that.

24 So what is that based upon?

25 MR. TROMBLY: My comment has been that in
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1 San Diego I personally witnessed where, in fact, a large
2 business has been classified as a small one, and they
3 hide under the back of an 8(a)

4 MR. KLEIN: Is what you're saying that an 8(a)
5 contractor was awarded a contract and is actually
6 allowing a large business to perform the contract? Is
7 that what you're saying?

8 MR. TROMBLY: Yes.

9 MR. KLEIN: Well, that's a different story.

That problem is with that particular contractor. An 8(a) firm, by statute and by regulation, is required to perform the work. If that's not being done, that's a problem of the with that entity you should look into that. That's different than saying size standards are being incorrectly used. That's a totally different issue.

MR. TROMBLY: When the issues are self-certification, when you allow self-certification to occur.

MR. KLEIN: As you know, there's a protest mechanism for small business set-asides. So if you believe a firm is not small who's being awarded a contract, you have the right -- and you should -- to protest that size standard to a contracting officer. The SBA will determine whether or not that is in

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accordance with its practices and procedures.

So that process is there for every contractor that's out there. If you think a large business is getting a contract, we don't like that. We should know. If fact, no one likes that.

So I'm not sure exactly what you want us to do in terms of our practices. If large businesses are getting contracts, we are against that as much as you are against that.

MR. TROMBLY: I want the SBA to implement its own enforcement policies. I should not be the enforcement of SBA's own standards.

MR. KLEIN: Thank you.

MR. JACKSON: A follow-up question on a different subject.

First of all, I want to clarify what Mr. Klein mentioned before, that SBA doesn't have any proposal out. We do have comments from a number of companies and associations through advance notice of December 3rd, 2004, and testimony at other hearings to consider higher standards. But we don't have anything specifically proposed.

We also don't have any anything specifically proposed on grandfathering. As Mr. Klein mentioned, we received comments on that approach in certain instances

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that SBA should consider, but we don't have any specific proposal for a five-year grandfathering or for any period.

I wanted to ask you a question about grandfathering since you opposed that. The reason we put that out for comment was the commentators to the earlier proposed rules were concerned that, as SBA tried to simplify size standards, that we wanted to have a neutral impact on small business eligibility.

But in many cases in which industries vary and companies' practices vary, a company of \$6 million may have 40, 45 employees, or it may have 50 to 60 employees, depending on how it's structured, the mix of their skilled work force.

And a lot of companies that would propose a 50-employee size standard for size standards that were before 6 million or turned to 6 million felt that they were losing their eligibility, not because we revealed the standard but just to attempt to simplify standards.

And the situation SBA was to consider again

21 going to the number of employees, a company that is
22 currently small under the small business size standard
23 will move to a number of employees, let's say, 50 again.

24 But if a company had 51, 55 employees, do you
25 think it's reasonable for SBA to consider some limited

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1 period of adjustment for those companies?

2 MR. TROMBLY: Sure, absolutely. And if I'm a
3 small business owner and I work my way out of the size
4 standards, that's a good thing. That means I'm no
5 longer a small business and have done something correct.

6 MR. JACKSON: A limited period of adjustment
7 you would not --

8 MR. TROMBLY: Sure.

9 MR. JACKSON: -- feel uncomfortable with?

10 MR. TROMBLY: Not a bit.

11 MR. JACKSON: Okay. Thank you.

12 MS. MALLWITZ: Good morning. I feel like I'm
13 already in a fish tank, perhaps, because I'm going to
14 give a somewhat different viewpoint from my predecessor
15 speakers.

16 My name is Marilyn Mallwitz, spelled
17 M-a-l-l-w-i-t-z. I'm the senior vice president of
18 CMI Management, Incorporated, in Alexandria, Virginia.
19 Thank you for the opportunity to present our views on
20 the size standards issue as presented in the ANPRM.

21 CMI is a small, minority-owned facilities
22 maintenance and records management business with average
23 revenues for the past three years of 17-and-a-half
24 million dollars.

25 In 2003 we had the good fortune to win a \$400

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1 million records management contract which is a five-year
2 BPA during a small business limited competition based on
3 GSA schedule 36.

4 Up to that point, our revenues were in the \$3
5 to \$3.5 million range, and our current primary NAICS
6 code is revenue based. As a result of winning this
7 contract, our revenues in 2004 increased to \$46 million.

8 However, approximately 48 percent of the work
9 and the revenues generated go to a large business
10 subcontractor, leaving us with approximately \$23,500,000
11 in annual revenues from that contract.

12 One area of the current system that we believe
13 does not work well and should be addressed as a change
14 to the existing size standards is the issue of
15 subcontract dollars. As a small business prime
16 contractor where only \$23.5 million worth of the work is
17 performed directly by the small business prime, it is
18 unfair to the small business to count the \$46 million as
19 small business revenue.

20 To illustrate the difference that one small
21 change would make, our current three-year average of
22 \$17.5 million would drop to \$10 million if we didn't
23 have to count the subcontractor's portion as part of our
24 average revenues.

25 I might add that I have heard comments to the

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1 effect that a small business does not have the
2 capability to handle such a large contract and must rely
3 on a large business for assistance. I assure you that
4 is not true in our case.

5 In fact, another company filed four protests to

6 the Small Business Administration and the General
7 Accounting Office -- it was called then -- claiming just
8 that we were just that, and we were able to disprove
9 their claims.

10 we have been and continue to be a prime
11 contractor in every sense of the word. We wrote the
12 proposal. We defended the protests. We paid the
13 lawyers. We obtained our own financing, and we built
14 our own infrastructure to handle this opportunity.
15 Granted, it was like drinking from a fire hose for a
16 while, but the contract is running smoothly, and we are
17 very much in control.

18 As a result, we look with dismay on the
19 potential threat to require small businesses to
20 requalify as small businesses for each option year on a
21 contract which is based on a GSA schedule. To do so
22 would not only cause us to be ineligible for the next
23 option year on our already hard-won BPA, but would
24 require the government to have to recompetete the
25 contract.

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1 As a result of the loss of this contract, at
2 that point we would again be back to our original \$3 to
3 \$3.5 million size and back to small business size
4 capability.

5 We thought the purpose of providing set-asides
6 for small businesses was to allow them to develop and
7 grow so that they could become large businesses at some
8 point.

9 Further addressing the government's position,
10 if SBA takes the position that small businesses must
11 requalify for each option year, contracting officers
12 will have no incentives to advertise any long-term or
13 large opportunity to small business that might cause the
14 small business to be disqualified after the base year or
15 the first option year since they will only be making
16 more work for themselves when their numbers have already
17 been cut to the bone.

18 With so much bundling of contracts to make them
19 only feasible for large business, this appears to be yet
20 another ploy to encourage bundling of contracts to the
21 detriment of small businesses.

22 Further, on behalf of the facilities
23 maintenance industry, whose primary NAICS code is
24 561210, and based on annual receipts, our industry is
25 already expected to be severely impacted by the proposed

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1 changes if a employee-based standard is adopted.

2 Because the very nature of much of our business
3 is already affected by seasonal requirements, such as
4 grass mowers are not needed in winter and snow plow
5 operators are not needed in the summer, we must operate
6 with numerous part-time employees, which currently are
7 counted in the same manner as full-time employees.

8 Additionally, these employees are fairly
9 low-paid workers who generate far less in revenue than
10 higher-paid management consultants and information
11 technology workers.

12 To further exacerbate this situation by basing
13 their size on an employee count that is already stacked
14 against them seems unconscionable for an agency tasked
15 with looking out for small businesses.

16 To illustrate my point, we have a very small

17 information technology element in our company -- three
18 people. Those three people with salaries of \$90,000 to
19 \$100,000 per employee, working on a three-month project,
20 generated approximately \$25,000 in profit for the
21 company.

22 This is in sharp contrast to the rest of our
23 business and the profit margin that is typical for our
24 industry. On those projects, employees usually are paid
25 \$10.00 to \$15.00 per hour, and our profit margin is

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1 usually about 5 percent.

2 Using that analogy, it would take a minimum of
3 16 of our employees working full-time for a year to
4 generate the same \$25,000 in profit as we received from
5 our information technology project in three months.

6 For that reason, if no other, we encourage the
7 SBA to remain with and increase the dollar-size standard
8 for this and similar industries.

9 I have one other point that I will drop because
10 I ran out of time.

11 MR. JACKSON: Do you have written testimony?

12 MS. MALLWITZ: Yes, I have, and I gave a copy
13 of it to Mr. Klein already, and I can give you this copy
14 if you like.

15 MR. JACKSON: You mentioned that you felt SBA
16 should not count subcontracts in determining the receipt
17 size of the business. Currently, as you know, we look
18 at the gross revenues of business or gross receipts in
19 looking at the size.

20 It's a similar question that I asked earlier.
21 In terms of an accounting system, how easy is it to
22 identify those subcontracts, or is that easy to
23 manipulate? That would be a concern that SBA would
24 have, and it's one reason we try to limit our
25 calculation on gross receipts as opposed to trying to

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1 look more deeply in terms of certain types of
2 subcontracts.

3 MS. MALLWITZ: No, it would be very easy for
4 us. I think any of us who have implemented the
5 "Deltech" system or most of the other
6 government-approved systems would have no problem in
7 identifying how many dollars are going to a
8 subcontractor on any of our contracts.

9 MR. JACKSON: If SBA were to take that
10 approach, would it be fair to one company that does less
11 subcontracting than another company? Two companies may
12 do the same level of contracting and generate the same
13 level of revenues, but in one instance the company does
14 more subcontracting, and it would be considered small
15 and the other one that does less is not.

16 How would we resolve that dilemma?

17 MS. MALLWITZ: That's a good question as to how
18 you would resolve it. But revenue is revenue to a
19 company, whether it comes from, you know, a prime
20 contract where they're only doing, say, 51 or 52 to 55
21 percent of the work and another vendor doing 100 percent
22 of the work, the same amount in revenue is the revenue
23 to the company.

24 But when you're paying out half of it almost to
25 a subcontractor, then it seems unfair to the company to

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1 be penalized for that simply because they were fortunate

2 enough to win a large contract.

3 MR. KLEIN: These standards today have been set
4 at levels that take into account revenue from all
5 sources.

6 MS. MALLWITZ: Yes.

7 MR. KLEIN: If we start excluding subcontracts,
8 I would expect the dollars levels would go down.

9 MS. MALLWITZ: Absolutely. As I mentioned,
10 ours would go down immediately this year from \$17.5
11 million average to \$10 million.

12 MR. KLEIN: The size standards themselves --

13 MS. MALLWITZ: So the size standard themselves
14 would go down?

15 MR. KLEIN: Because the size standards are
16 placed at levels where we look at small business's total
17 revenues. So I would expect -- and Gary is the
18 expert -- but I would expect the size standards
19 themselves to go down if we excluded small businesses
20 based on their subcontracting issues.

21 How would that affect you?

22 MS. MALLWITZ: That would also be still
23 detrimental to us -- is what it amounts to -- because we
24 are unfortunately in the situation, along with a lot of
25 other companies, where we're in competition with the

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1 behemoth companies -- the Lockheed Martins, the Boeings,
2 the Johnson Controls -- you know, it goes on and on --
3 the huge companies.

4 Once we graduate out of the small business
5 category, because there is no intermediate level, we
6 find ourselves in that situation, and usually we end up
7 having to sell out to one of those companies because we
8 have no choice because we've become too small, again, to
9 be able to compete with them but yet, for a year or two
10 because of the averages of our income, we are too large
11 then to get a small business set-aside again.

12 MR. MANALISAY: I had a question that's again
13 in this era of large contracts and we do see contract
14 bundling and contract consolidation.

15 In the dilemma that you present in winning
16 contracts of that magnitude, I guess my question is more
17 of which do you prefer? Do you prefer pursuing larger
18 contracts knowing that this puts you at possibly
19 outgrowing your size standard but you're a prime
20 contractor, or do you prefer pushing yourself back to a
21 subcontractor role, knowing that you won't go over your
22 size standard?

23 MS. MALLWITZ: Our preference is always to be
24 the prime contractor as opposed to being a subcontractor
25 because frequently, if you're a small business and

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1 you're a subcontractor, again, to one of these very
2 large companies, they do not necessarily treat their
3 small businesses well.

4 They may put you on their team to win an
5 opportunity, but when it comes time for implementation,
6 most of them will go back and tell the government that
7 they cannot find adequate small companies to perform the
8 work on the contracts that they have won even though
9 they have made that commitment to the government in
10 many, many of those contracts.

11 And if as a small business, you call them or if
12 you're on that team and on the proposal in the first

13 place and you say to them, "But we were on your team.
14 We were one of the reasons that you won the contract.
15 You even stipulated that to us as we were putting our
16 teaming arrangement together."

17 And they say, "Well, the situation has changed
18 now, and as a result, we don't have to live up to that
19 responsibility."

20 There's no one policing them is essentially
21 what it amounts to.

22 MR. KLEIN: Thank you.

23 Sarah Hazel.

24 MS. HAZEL: Good morning. My name is
25 Sarah Hazel, last name spelled H-a-z-e-l. I'm here

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1 representing GC Micro Corporation. We are an 8(a)
2 graduated company in the IT industry, and I'm here to
3 voice our concerns about the SBA's small business
4 program.

5 In 2002 the GAO launched an investigation based
6 on information provided by the Americans Small Business
7 League president, Lloyd Chapman. The GAO found billions
8 of dollars in small business contracts have been awarded
9 to large businesses.

10 The SBA was then forced to remove these names
11 from PRO-Net, the SBA's very own small business
12 database. Firms such as Nike, AT&T, Hilton Hotels,
13 Office Max, and Office Depot were listed as small
14 businesses.

15 Yet, according to the U.S. Census Bureau,
16 statistics show 89 percent of all U.S. firms have less
17 than 20 employees and the average American firm has
18 approximately 12 employees.

19 Based on the numbers, we are not in favor of a
20 multitiered size standard. We believe size standards
21 should be established industry by industry. The size
22 standard for the IT industry wholesale trade category,
23 NAICS Code 421430, is 500 employees while the size
24 standard for all other wholesale trade is 100 employees.

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1 This size standard was arbitrarily changed from
2 100 employees to 500 employees a number of years ago.
3 We request the size standard be returned back to 100
4 employees.

5 The SBA received well over 3,000 comments in
6 favor of returning this very size standard back to 100
7 employees during the 2004 comment period. We feel that
8 a multitiered system will only further complicate the
9 contracting process for appropriate personnel.

10 In regard to VCCs, we believe there should be
11 no exclusions for affiliation from venture capitalists
12 in size determination, for eligibility, for SBIR, or
13 small business innovation research programs.

14 We are not in favor of grandfathering. This
15 only allows large companies to continue to represent
16 themselves as small business through grandfathered
17 contract vehicles.

18 MR. KLEIN: What do you mean by
19 "grandfathering?"

20 MS. HAZEL: It's my understanding that
21 grandfathering will allow large --

22 MR. KLEIN: What do you envision -- I mean at
23 different hearings people have used "grandfathering" in
different contexts. I want to understand what you're

24 objecting to, just so we know.

25 MS. HAZEL: I'm objecting to grandfathering
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1 because it will allow large businesses to continue to
2 represent themselves as small businesses through "GWAC"
3 contracts, et cetera.

4 MR. KLEIN: Okay. The grandfathering that we
5 were asking comments for was what Gary mentioned before.
6 Because of the proposed change in March 2004 from
7 receipts-based to employee-based standards, we tried to
8 remain neutral, as you say, in terms of the small
9 business effect. So if you're small today, we'd want
10 you to be small under the new standard.

11 However, during that crossover, through the new
12 terms if somebody fell out from being small, even though
13 they met the \$6 million size there, for instance, they
14 had 55 employees versus 45, they're now other than small
15 under the proposal.

16 And in response to that, we received comments
17 that that wasn't fair, that SBA should allow a
18 grandfathering of those firms who are small today under
19 the size who, because of the crossover, they would not
20 be.

21 with that definition of "grandfathering," would
22 you oppose that firm who's small today with \$6 million
23 who changed to a 50-employee standard, or would you want
24 them to be ineligible for that contract? would you want
25 them to transition into that?

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1 That's the question we're asking.

2 MS. HAZEL: Using that definition of
3 grandfathering, I'm opposed to it.

4 And that doesn't come into my time.

5 We are not in favor of grandfathering, as I
6 said. This will only allow large businesses to continue
7 to represent themselves as small businesses through
8 grandfathered contracts, as I said before.

9 In fact, I was most concerned by the report and
10 the news that the SBA's own inspector general had
11 recently released the results of three investigations
12 that found the SBA was reporting awards to large
13 businesses as small business awards.

14 We feel that this is supported by --

15 MR. KLEIN: Again, we've heard these comments
16 several times from the same group. I wish you would
17 please state the facts as they really are.

18 The OIG and GAO have all found that firms that
19 have grown to be other than small are being counted as
20 small business contracts. That's the issue. And if
21 that's what you're referring to, that's fine. But
22 please don't say that SBA is giving awards to large
23 businesses. Thank you.

24 MS. HAZEL: May I read the excerpt from the
25 515?

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1 MR. KLEIN: why don't you just --

2 MS. HAZEL: "One of the most important
3 challenges facing the Small Business Administration and
4 the entire federal government today is that large
5 businesses are receiving small business program awards
6 and agencies are receiving credit for these rewards."

7 That comes from Report 515 released by the
8 SBA's own inspector general report.

In conclusion, 98 percent of all American firms have less than 100 employees. These are the firms that Congress intended to benefit from the Small Business Act. These are the firms where most Americans work. These are the firms where most of America's tax revenue is collected. These are true American small businesses that do not want or need grandfathering, a tiered system, or exclusions from the affiliation rules of the venture capital companies.

I'd like to thank the panel for the time to give my testimony.

MR. ALVARADO: Sarah, not apropos to the topic of this hearing, and be gentle with us on this question.

Life after the 8(a) program, how has that been for you, and particularly what might have been better? We always seek to improve our programs.

what might have been better in your 8(a)

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experience that might have put you in a better position for your post 8(a) life?

MS. HAZEL: I'm lucky enough to work for an amazing company because of the fact that we have graduated from the 8(a) program, we have amazing relationships with federal agencies and prime contractors.

Unfortunately, I wasn't with the firm during its 8(a) status. I know every day we run into procurement personnel that could be better educated about what set-asides are, how they work with SDBs, 8(a)'s, et cetera.

I'm not sure that I can provide you with any information. Maybe you should ask somebody who has a little more experience with that.

MR. ALVARADO: Thank you.

MR. JACKSON: Just a couple of things. They're really not questions but just to inform you of certain things. First of all, in the OIG audit of SBA procurements, we found that originally there were four companies that weren't small businesses.

I'm sorry. My voice doesn't carry. So I need this.

I don't have a question so much as just to inform you of a couple of things that SBA is doing in

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light of your comments that I'd like to inform you about and the audience.

I would like to follow up with what John said. The reason IG reports on SBA procurements that the companies that were getting contracts as large businesses is that they were originally small when they received the contract. When orders were placed against those contracts, the companies had either grown to be large or were acquired by large businesses.

We did publish a proposed rule in April of 2003 to require a recertification to more accurately report on the small business status of those companies. So we do have policies to address some of those issues.

Our final action on that is very near completion or literally at the -- we're past "the dot the I's and cross the T's" stage. But there is a review process that we have to go through for rule making.

So again, a lot of these issues are related to what happens when a small business is performing over

the life of the contract and how that is reported.
There are some other issues that we're trying to deal
with separately that have more consequences than just
reporting.

Secondly, in the advance notice, we mentioned
that in terms of the size standard factors, that's

mainly directed at companies that are distributors or
resellers to the federal government. We stated that we
are conducting an individual review of that size
standard. That's apart from the issues that we are
looking at here.

My staff has completed an analysis that I'm
currently reviewing to look at what is a more
appropriate size standard. Obviously, no decision has
been made. But as soon as we do get the proposal out, I
will certainly inform you and would like you to comment
on our proposed change. It will describe the approach
that we looked at in looking at size standards.

But again, just to let you know that a lot of
these issues we are dealing with one way or another.

So thank you for your testimony.

MR. KLEIN: Robert Myer.

MR. MYER: Good morning. My name is Robert
Myer, M-y-e-r, spelling. I'm with Robert Myer
Consulting doing business as Express Personnel Services
of Baton Rouge, Louisiana, and Gulfport, Mississippi.

I want to thank you for taking the time to let
me address this panel here in L.A.

I have been a small business owner since August
of 2001 and an Express franchisee for four years. The
reason I'm here all the way in L.A. is because I was at

a business summit a couple of weeks ago down in
New Orleans where NASA and SBA was there talking about
how to do business with the government and NASA, in
particular, because there are two facilities in the area
that I work.

When I was told that -- found out that I wasn't
eligible for some of the SBA benefits such as loans and
NASA contracts as my peer groups were, I decided to buy
my own ticket and come here. And I appreciate y'all
giving me that opportunity.

What I respectfully request is that SBA should
consider these following factors when looking at my
business status as a franchisee.

I bear the entire risk of financial loss for my
business operations. In fact, in four years I have
written off over \$50,000 in bad debt from both small
businesses and large businesses who didn't pay their
bills.

I retain the majority of the profits from my
relationship with Express; in other words, a 60-40
split. I retain 60 percent; they take 40 because they
do the back-room operations, accounting, and payroll
services.

I maintain the day-to-day control of my
business operations. I hire people for my own staff. I

hire the temporary staff that I place. I hire the
permanent staff that I place. I pay all the benefits to
my employees.

The fact that I have a relationship with

Express does nothing to get us any kind of break on benefits, which is a shame in itself too. But that's a different story for a different panel, I'm sure.

I provide the financing for my company without any recourse for indebtedness or repayment to the franchisor. And there's no common ownership or management between the franchise owner and myself. I basically use them to payroll our temporary staff employees and to keep records.

I'm in the people business, and I provide workers to client companies along the Louisiana and Mississippi coasts. As I said, I contracted with Express to give us the back office support and operations, payroll and billing services. These are services that I can buy from other, more expensive venues, other unproven companies because this is a proven operation.

Dealing as a franchise in the staffing industry as one entity is not completely accurate, I feel. It appears, you know, because of the rules, I may not be a small business owner.

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But there are several other points that you can consider too. As an independent corporation, I have my own federal ID number, state and local tax identification numbers, workers' compensation, state taxes.

My business is separate and distinct. As I said, I oversee my day-to-day operations. I have the sole responsibility for all the recruiting, training, and placement of my temporary staff. All the costs -- background checks, drug tests, everything that I have to do to do my job is my responsibility.

Finally, I'll talk a little bit about the respective role of the franchisor in how my business is doing. Because we are in the people business and not an over-the-counter business, my business does contract with -- through our franchise agreement to let them do the account receivables. As I said, I retain the majority of that; they take a percentage for doing that work.

As an independent franchise owner, I have the sole responsibility for credit collections. As I said, I have lost a lot of money off of that, if a client doesn't pay me. In fact, three weeks after buying the second office -- the Mississippi office had a bankruptcy, and I purchased the office through another

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Express owner, and the company and I -- there was no recourse from Express because that money was gone. I didn't get paid, but a deal is a deal. And so there's nothing there.

I'm down to one minute. So let's see what the most important thing is.

Basically, I'll just say this in conclusion: I would like to -- my plea to the SBA is that with the rate of small business failures in America, the SBA should be looking at ways to help small business stay in business. And if franchising is an opportunity to help small businesses through knowledge and paid-for expertise, then SBA should support that.

MR. KLEIN: As I said before, we have seen the Express franchise agreement. So we understand that

16 situation.

17 Do you know anything about the industry in
18 general? Is the situation similar where the franchisor
19 requires the franchisee to enter into these agreements?
20 And the payroll, for instance, is that -- in the
21 industry itself, does the franchisor often require the
22 franchisee to do that other than Express?

23 Do you know anything about that situation?

24 MR. MYER: Basically, I can enter into -- I
25 know franchise owners who have been with Kelly or

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1 Manpower, and after five years, when their franchise
2 agreement comes up, they've decided to go do it on their
3 own. So those --

4 MR. KLEIN: That's a good question. In the
5 Kelly situation, does Kelly require the franchisee to do
6 the same things that Express requires you to do?

7 MR. MYER: Well, I can't speak to their
8 specific contracts, but what I can speak to is that from
9 different avenues, different franchise agreements, there
10 are ones that costs are less and ones that costs are
11 more. There are opportunities for people to either be
12 within a franchise system or independent, if they want
13 to. And there's multiple services that you can purchase
14 outside of the franchise agreement or within the
15 franchise agreement.

16 MR. JACKSON: Mr. Myer, we have heard testimony
17 from other franchisees of Express Personnel, and one
18 area that we have not asked -- and I'm unclear on -- is
19 hearing you mention, as well as others, that -- you say
20 that you pay the benefits to your employees.

21 My understanding is that the franchisor is the
22 employer of record. You go to the franchisor for the
23 back-room operations.

24 In terms of payroll, how do you pay your
25 employees? Is that through the franchisor, and how is

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1 it that you pay the benefits? Do you have different
2 benefit levels than what another franchisor might have?

3 MR. MYER: Let me give you a point of
4 clarification. I have to have a staff -- Robert Myer
5 Consulting has to have staff. I have ten employees. So
6 I pay benefits to them.

7 Then we have the temporary payroll in which
8 we -- the first part of your question was, you know, how
9 do they get paid. Well, we process -- they process the
10 payroll. The checks are sent back to us -- actually,
11 not sent back to us. We print the checks in our office.
12 We're totally responsible for those checks.

13 In fact, one time we lost five checks. And did
14 Express eat that? No, no, that was my baby. So in
15 other words, we're totally responsible from a financial
16 standpoint, period.

17 Now, the other part of your question, the
18 benefits. Express as a corporation for temporary
19 employees, we can purchase those benefits to give those
20 employees. And they do split it with us just like the
21 60-40 split I mentioned earlier.

22 If an employee earns some benefits, vacation
23 time or whatever, I pay my portion of that, and Express
24 pays the difference.

25 MR. ALVARADO: Let me just ask for the purposes

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1 of the greater group -- and I'm assuming that John, in
2 particular -- this particular franchise actually has
3 been reviewed, the franchise agreement all the way up to
4 headquarters also?

5 MR. KLEIN: Yes.

6 MR. ALVARADO: You should know that, as a
7 general rule, we finance throughout the country
8 franchise businesses every day of the week. And the
9 question always is which franchise is eligible -- the
10 franchise agreement itself. And it's been mentioned
11 several times already that the principal rule is that
12 the business, which we have to find to be independent,
13 has to have the right to profit and bear the risk of
14 loss.

15 And that sounds like a trite thing, a simple
16 thing, and obviously Mr. Myer and Mr. Flood believe that
17 that is the case with their particular agreement. And
18 I'm assuming that that's an ongoing review that we need
19 to take a closer look at.

20 But just so as not to give you the impression
21 that we don't finance franchises -- and those of you
22 that have an interest in that area or know other people,
23 what we typically will ask someone to do, if you're
24 looking for financing, is to get that agreement to us so
25 that we can conduct -- and these reviews are done across

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1 the country in all the field offices -- so we can
2 conduct that review, which is, again, not germane
3 exactly to your situation, but more generally.

4 MR. FLOOD: Could I add a comment to
5 Mr. Jackson with regards to offering benefits to our
6 associates and not our core staff. We have the
7 opportunity to either do that or not. It is not a
8 requirement of the franchise agreement.

9 If we choose as an office owner to say, "No,
10 we're not going to offer benefits" -- medical, holiday,
11 vacation, 401K, we have the right to say, "No, we're not
12 doing that. That's not part of our business plan."

13 MR. KLEIN: Thank you.

14 Frank Evagues.

15 MR. EVAGUES: Good morning. My name is
16 Frank Evagues, and that's spelled E-v-a-g-u-e-s, and I'm
17 president of Tactical Displays, Inc. We're a small
18 veteran-owned business located in Orange County,
19 California, and we have only five employees.

20 We design and build and test and manufacture
21 display monitors and systems for the military
22 marketplace. We have been in business for ten years.
23 And thank you for the opportunity to speak on the issues
24 affecting small businesses and thanks to the American
25 Small Business League for making us aware of the issues

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1 in this hearing.

2 Small businesses are critical to the economic
3 success of the United States, and decisions made by the
4 Small Business Administration can affect the success.
5 And I will not dwell on the statistics related to small
6 businesses but move to the issues at hand, in particular
7 grandfathering.

8 We are not in favor of grandfathering. It's
9 difficult enough competing in this complex military
10 market without having to compete with large
11 corporations. And in addition, we would like to keep

12 the program simple. Small business should be defined as
13 100 employees or less. And it may be straightforward to
14 you, but it's confusing to me as to what --

15 MR. KLEIN: What business are you referring to,
16 100 employees or less? In what industry? All
17 industries across the board?

18 MR. EVAGUES: I'd say so, yes. And it's
19 confusing to me. It may not be confusing to you. But
20 yesterday I downloaded a solicitation from the Federal
21 Business Opportunity, and it says a small business
22 set-aside, a thousand employees.

23 So I'm confused as to what a small business
24 really is, and I see differences all the time. Small
25 businesses do not have the resources to lobby government

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1 or prime contractors to make the procurement for a small
2 business set-aside. They have the requirement to set
3 aside this business and should do so without
4 intervention in small businesses.

5 Many large corporations and government offices
6 pay lip service to the goals of small business
7 set-asides. There needs to be enforcement and penalties
8 imposed.

9 We're seeing in more and more large
10 corporations friends teaming with other friends, and
11 they keep the business in house. There is no allocation
12 for small businesses. These large corporations -- many
13 of them have subsidiaries that compete with small
14 businesses. So when they win a program, the business
15 never flows down.

16 And I was told by procurement people in one
17 large corporation when I was trying to gain entry into
18 the company that "We have enough vendors." So I run
19 into these kinds of things.

20 In addition, there are large foreign companies
21 that set up offices in the United States, and they
22 compete with substantial resources against small
23 businesses. They have the resources to lobby
24 procurement agencies in their favor. So not only are
25 small businesses losing out on government contracts, but

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1 the business is going overseas. We need more
2 enforcement and penalties.

3 Business that can easily be a small business
4 set-aside is not because of lobbying by larger
5 corporations. As an example, we competed on a
6 government program many years ago. We won. And our
7 equipment was qualified along with the system. When the
8 production award came along, the business was
9 recompeted.

10 You know, we won the program originally on a
11 competitive basis. But when they went to production, we
12 recompeted it, and it was not a sole source, a small
13 business set-aside. It was recompeted.

14 And then at one point we heard the request for
15 a quote for production, and when it was being released,
16 it was in the legal department. And we suspect that
17 lobbying was going on against small business.

18 And again, our limited resources don't enable
19 us to compete with larger companies. We can't have
20 people sitting there and talking to procurement people
21 trying to make these small business set-asides or
22 fighting against these larger corporations.

23 Small businesses provide a service to the
24 marketplace, in my case, the military marketplace. We
25 offer very competitive prices, on-time delivery,

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1 high-quality product, and services unmatched by large
2 corporations.

3 We typically design custom products to fit the
4 specific application at no cost to the military. We
5 work with the customer to ensure a perfect match, and
6 all of this is done in real time. Larger corporations
7 have a bureaucracy that can't provide that service,
8 especially at our cost.

9 So we need the support of the Small Business
10 Administration to ensure we get a level playing field.
11 We don't need grandfathering or complex size standards.
12 The government is getting the best value from small
13 businesses, and if we are not supported, this is a
14 disservice to the government.

15 We need help in competing against large
16 corporations. Thank you.

17 MR. KLEIN: I have a few comments. You said at
18 one point that subsidiaries of large businesses were
19 competing against you as small businesses. Are they
20 competing --

21 MR. EVAGUES: No, they're not in small
22 businesses. No, they're not doing that. They have
23 subsidiaries that have equivalent capabilities, and that
24 business is never released outside of that contract.

25 MR. KLEIN: And the foreign companies are also
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1 competing not in the small business arena, but competing
2 outside the arena as well?

3 MR. EVAGUES: Yes.

4 MR. KLEIN: We also share your concerns
5 regarding small businesses not getting a fair share of
6 contracts. As you know, we are always working for that,
7 and Nick can talk about what PCRs do daily, try to make
8 contracts for small businesses. But it's a tough fight,
9 and we agree that there are things that can be done.

10 MR. EVAGUES: Appreciate it.

11 MR. MANALISAY: For the general audience, I'll
12 just let you know that in SBA's Office of Government
13 Contracting, we have a cadre of approximately about 40,
14 50 across the country. Officially, they're called
15 procurement center representatives, the PCRs.

16 And one of their jobs and responsibilities is
17 to work with the federal agencies that you mentioned and
18 identify those contracts that can be set aside for
19 exclusive small business participation or one of the
20 other socioeconomic programs which, for instance, may be
21 an 8(a) program or historically underutilized business
22 zones, small business concerns, or service-disabled,
23 veteran-owned small businesses.

24 One of the things certainly -- and this is not
25 a pitch or anything -- but just factually the SBA has
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1 undergone downsizing. And we went from somewhere around
2 125, 130 personnel across the country to where we're now
3 in the forties, fifties total across the country. So we
4 have dwindling resources.

5 What does that mean? I think one of the
6 comments -- and, sir, I apologize, but I don't know if
7 it was you -- but it was mentioned that, by regulation,

8 federal agencies are required to set these contracts
9 aside. And I think, just like John said, we do echo a
10 lot of the sentiment that there is certainly lobbying.

11 There's political lobbying that goes on.
12 There's large businesses that certainly do what they can
13 to keep contracts from being set aside for small
14 business. But that's the federal agencies'
15 responsibility; it's the SBA's and the PCR that are
16 available to do the oversight.

17 And I know we are doing our best, but we are
18 also very concerned with a lot of the contracts so that
19 we do see the way the contract strategy is formulated
20 and where it finally ends up.

21 MR. KLEIN: If you become aware of contracts
22 that you believe should go to small business but are
23 being prepared for a large business, you know, contact
24 Nick if you're in the area because he can fight for you
25 on your behalf to try to get this contract enforceable

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1 if possible.

2 MR. MANALISAY: Thank you, John. What I will
3 add to that is, if there are those opportunities out
4 there that you feel small businesses can't compete --
5 and it can be a small business set-aside -- the best way
6 to do it is come to the website, sba.gov, and we have a
7 small business set-aside alert. And so you can just
8 enter the information into the Internet. It is directed
9 to the correct area offices.

10 There are six areas across the country, but
11 it's directed to the right person. It gets there
12 quickly, and we can hopefully work something out where
13 we could increase small business participation.

14 Thank you. Excellent comment.

15 MR. KLEIN: Thank you, Nick.

16 MS. MICHEL: Monique Michel, M-o-n-i-q-u-e,
17 M-i-c-h-e-l. I'm the president of Newcom Telephone
18 Company, Incorporated. Started my business 21 years ago
19 in Las Vegas as a communications contractor and was
20 writing to the SBA program in 2001.

21 And in the last two years, I brought on general
22 contracting and electrical contracting to try to get
23 some resources going in getting some set-aside contracts
24 because as a communications contractor, it just wasn't
25 happening with 8(a) set-asides.

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1 One of my biggest obstacles are the size
2 standards in my trade, and it's 28 million. All right.
3 So I'm just a speck in a business in that range because
4 I was only doing 900,000 until last year when we broke a
5 million last year.

6 When we try to compete with companies in that
7 range with bonding and the capabilities that they have,
8 there's a big disparaging field there for us to go
9 compete with them.

10 So in the SBA you have some very good
11 programs -- Mentor-Protege is one of them -- to try to
12 help us work with larger businesses to get these
13 contracts, which I know a lot of 8(a) companies have
14 been able to do so.

15 And in the four years I've been trying to get
16 this on, I kind of notice a pattern that with a lot of
17 these companies who have a Mentor-Protege situation set
18 up, it seems to be like an internal -- the bigger

19 companies who have been in the government game for 10,
20 20, 30 years finding someone eligible for an 8(a)
21 contract, helping them get an 8(a) contract, an 8(a)
22 set-aside status, and then they plant their office in
23 their own company. And basically, the large company is
24 doing everything.

25 I have worked as a subcontractor, set up 8(a)

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1 set-aside projects in the millions, and I never see
2 anybody from the 8(a) company but from the parent
3 company. You know, they're project managers, and that's
4 on their business cards. Call their accounting
5 department, you get the major company's accounting
6 department.

7 You bring this up to the SBA, and they say,
8 "well, it's the contractor's obligation to lease these
9 jobs and make sure they're doing a percentage of the
10 work and things are being done correctly."

11 And, you know, if you go there and you start
12 being the scapegoat and tell everybody what's going on
13 and try to get your nose into it, you don't get a
14 contract from anybody because you're going to be the
15 troublemaker over here.

16 You might have to go to these people for a job
17 as a subcontractor. So you're not going to want to be
18 well known as trying to turn them in, like police them.
19 And when you go to the SBA, they say it's a contracting
20 problem. Contracting is just trying to get their job
21 done.

22 So I do believe that the SBA needs to have a
23 little bit more of their policies on policing how things
24 are run. Last year I probably got a few set-aside
25 projects. They were decent to me. You know, we did

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1 \$800,000 in set-aside projects, and that's good for a
2 small vendor like --

3 MR. KLEIN: What kind of set-asides are they?

4 MS. MICHEL: They're 8(a) set-asides. And it
5 was with the air force base I had built a relationship
6 with for ten years. And then we do a lot of service
7 work with the Veterans Administration. And we have
8 outstanding reports. Never have problems. So
9 everything across the board.

10 But these small, little contracts, they start
11 getting heat for putting it on credit cards and using us
12 too much, but then they turn around and these big
13 companies give them 6, \$7 million, same base. And we're
14 not getting too much work.

15 So I kind of don't understand the platform
16 there. When we might get 60,000 a year out of this
17 place, and they get 6 million, and we're getting too
18 much work.

19 So the size standard, I don't think you can go
20 by employee based, especially in contracting, because
21 when I'm a sub for somebody who's a GC contractor, they
22 may have 20 employees, and they're doing \$100 million
23 worth of work a year because they're doing everything as
24 subcontractors and they're just managing the contract.

25 So if you would have me compete with them on a

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1 size standard, they're as big as me employees-wise, but
2 of course their resources are way above my level.

3 So I would really look at the type of business.

4 You can't go gross receipts with contracting. And as
5 far as the employee status, I know on government jobs
6 there's a lot of game playing with employees and
7 certified payrolls. So how do you make sure how many
8 employees they really have? How are you going to police
9 that if you're not auditing these people on a regular
10 basis?

11 MR. KLEIN: You know, before somebody spoke
12 about excluding subcontract dollars. Would you disagree
13 with that?

14 MS. MICHEL: I would disagree up to a certain
15 point because I'm looking at some of these contractors
16 I'm telling you about, and I've heard they got
17 \$45 million in 8(a) contracts last year -- is one of the
18 people I'm working with, and they're playing this game.

19 All right. Well, if you get a \$400 million
20 contract, that's outstanding. Maybe you can exempt like
21 one five-year contract, but they shouldn't be able to
22 just pile on two or three more contracts if they got one
23 \$400 million contract.

24 Maybe exempt for one big contract so the agency
25 doesn't have to rebid it, and they still meet that size

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1 standard. They had it when they got the contract, and
2 they're good for it during that period of time. But I
3 don't think they should be able to go out and get other
4 2 to \$3 million contracts as a small business if they're
5 already doing \$400 million.

6 And, granted, you have subcontractors, but
7 that's all part of being a prime. You make a percentage
8 on that sub. So you're still making your money, and you
9 still have that contract.

10 So I do believe you should have some sort of
11 leeway for someone who's fortunate enough to get a big
12 contract and not throw them totally out of the game but
13 not allow them to continue on getting many new large
14 contracts if they've already got one. Share it. There
15 are so many of us 8(a)'s out there. Why should
16 everybody get -- or why should a few get dozens of
17 contracts and a few of us get nothing?

18 And I see a lot of that going on, and it's not
19 necessarily the quality of the work. It's usually
20 lobbying.

21 I work all the time. I don't have time to go
22 out there beating on doors and brown-nose and wine and
23 dine and do whatever people are doing to get these
24 contracts. And I've tried to figure it out. But we go
25 on the standard of the quality of our work.

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1 Thank you. I appreciate you guys giving us a
2 chance to talk about our issues. And thank you for all
3 the work you have done for us.

4 MR. JACKSON: I just have a question, and this
5 is a little outside my area. Mr. Klein would be more
6 knowledgeable than I'm. But I'm going to take the
7 liberty of asking you a question.

8 You mentioned that in some of the
9 Mentor-Protege agreements that you've seen, the large
10 companies are very involved in the 8(a) regulations.
11 I'm aware of that. The protege is required to be in
12 control of the contract. Now, there may be a question
13 about how that is administered.

14 But aside from that, do you have any

15 recommendations for how the regulations might be
16 modified to insure that the protege is more in charge?
17 I'm not sure if you're familiar with the regulations
18 per se, but --

19 MS. MICHEL: Yeah, I have had many meetings
20 with companies, trying to set up relationships, and I've
21 always been very up-front. I'm an honest
22 businessperson. I've been in business 21 years, and I
23 like to follow the rules. But I'm the one person who's
24 going to get caught if I do something stupid.

25 And what happens is I tell these gentlemen that

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1 I do want to work with them, learn, and do everything
2 that the spirit of the association has to offer. And I
3 think once they realize you're really going to be there
4 and do your job and be part of the deal and be
5 accountable, they don't really want to work with you.
6 They want somebody to send a paycheck to and don't want
7 to see you.

8 And one more point I'd like to make real quick,
9 if I could. Communication was my mainstay, and I spent
10 ten years building a rapport with the air force base
11 that I worked out of and just started getting contracts.
12 And behind closed doors, somehow a huge \$9 billion,
13 ten-year contract got awarded with eight prime
14 contractors. Five are the big boys, four small
15 businesses that are in the \$28 million size standard
16 which are all way up there. Go on their websites, they
17 have million and billion-dollar contracts.

18 This all happened back in September, and when I
19 went up to my SBA office, they had no idea it ever
20 happened. They had never heard of it. This is February
21 when I went to my SBA office. They came out of a small
22 SBA office in Alabama -- or a small air force base in
23 Alabama and their SBA representation when it went
24 through.

25 It's a mandatory contract that all

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1 communications and IT goes through this contractor for
2 all air force bases for the next ten years. I'm losing
3 work right and left, and so are hundreds and hundreds of
4 small businesses across this country. And it's very sad
5 that we have to get in bed with these nine big guys in
6 order to get any work on our air force bases. And the
7 GSA has actually set this up -- their GSA rep. It's
8 huge.

9 MR. KLEIN: Thank you. Belinda Guadarrama.

10 MS. GUADARRAMA: Good morning, gentlemen. I'm
11 Belinda Guadarrama. I'm the president and CEO of a
12 graduated 8(a) company.

13 MR. KLEIN: Could you please spell your name.

14 MS. GUADARRAMA: G-u-a-d-a-r-r-a-m-a. I'm here
15 representing the Northern California 8(a) Association
16 for Government Advocacy; the New Mexico 8(a)
17 Association; the Marin, Solano and Sonoma Hispanic
18 Chambers of Commerce.

19 And we're very concerned about the small
20 business program and the current small business size
21 standard proposal that's out.

22 We work very closely as a group of these
23 various organizations in what we can do to help small
24 businesses all across America. And as we look at the
25 various parts of the proposal that are out there, we are

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1 concerned about it.

2 We're concerned that it's actually taking --
3 it's trying to come up with a global solution for size
4 standards across the board for all small businesses
5 when, in reality, that's just not going to work.

6 I think, just based on the number of
7 individuals that have been up here today, when you look
8 at small businesses, we are in so many different areas
9 that to actually try to come up with something that's
10 going to fit everybody will not work.

11 Specifically looking at whether we should
12 supporting multitiered size standards, I believe the
13 multitiered size standard is something that you're
14 looking at and you're trying to look at how to redefine
15 small businesses across the board. We're completely
16 against multitiered size standards, particularly out
17 there that refer to ranges up to 1,500 employees.

18 Most of the small businesses that we see across
19 America cannot compete with 1,500 employees. They can't
20 compete with a thousand. They can barely compete with
21 500 employee. The statistics that have already been
22 cited earlier today clearly show that probably 98
23 percent of small businesses across America actually have
24 less than 100 employees.

25 Now, at the same time, when you look at some of

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1 size standards, some of these businesses need a very
2 large number of employees in order to actually be able
3 to do their business. If you look at environmental
4 remediation, they need hundreds, if not thousands, of
5 people when they're actually trying to work with the
6 Department of Energy.

7 If you look at CPA firms and if you look at a
8 lot of the other firms, they can't compete in those
9 types of categories. What we strongly suggest is that
10 you actually look at the size standards based by
11 industry, and based on the industry, then take comments
12 in terms of what you think within that industry would be
13 a reasonable size standard to try to work with.

14 In terms of working out whether it should be
15 receipt based or employee based, we generally favor
16 employee based because that is a, for a number of small
17 businesses, an easier number to work with.

18 And when you're looking at --

19 MR. KLEIN: You mean for services industry?

20 MS. GUADARRAMA: Yes.

21 Now, we run into the problem of part time
22 versus full time, and in that case, we're completely in
23 favor of switching it over to the full-time
24 equivalencies. We think that that's a reasonable way to
25 work with that part of it.

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1 As we look at the Small Business Act itself
2 that was passed in 1953, it specifically says that a
3 small business is one which is independently owned and
4 operated and not dominant in its field of operation. I
5 think you have a number of small businesses right now
6 that are quite dominant in the field that are continuing
7 to be small businesses.

8 In terms of the protest vehicles that the SBA
9 has out there, there are very, very many ways to try to
10 work around that. In terms of contract bundling, we

11 just have a problem across the board with the small
12 business program.

13 Specifically, one of the areas that you were
14 talking about was the current affiliation -- not the
15 affiliation -- the one on venture capital and whether or
16 not the venture capitals actually should be able to own
17 over 51 percent of the company and still actually be
18 looking at it as a small business. No, we are not in
19 favor of that. We firmly believe that if you are a
20 small business, you should be only 51 percent of that
21 company.

22 I find it hard to believe that for venture
23 capital companies that if they can't own 51 percent,
24 that they can no longer work with small businesses. 49
25 percent is a lot of small business to own and still be

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1 able to have a lot of input in what it is that that
2 company is doing. So we're very clear on that one.

3 Now, in terms of NAICS Code 421430, which is
4 the one for nonmanufacturing wholesale trade, I think
5 you already spoke to that, Mr. Jackson, and you are
6 going to be looking at that later on. We'll hold
7 comments on that.

8 In terms of recertification, we do believe that
9 there should be annual -- at the most, two-year --
10 recertification for small businesses. If you look at
11 other organizations that are out there, the National
12 Minority Development Council, which most of the small
13 businesses that are working outside of the federal arena
14 are members of, they have one-year annual certification
15 for small businesses.

16 If you look at SDB certification, that does
17 have three years. I have heard that five years is being
18 considered. That is such a longer time period than any
19 of the other certification programs that are out there,
20 that we're very much against that. We would be in favor
21 of one to two years at the most.

22 I know I'm running out of time; so I'm trying
23 to do this quickly.

24 In terms of grandfathering, we are not in favor
25 of grandfathering. Now, grandfathering -- I realize

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1 that there are different definitions that you're looking
2 at. You're looking at the small business having
3 exceeded the small business size standard when making a
4 change to the small size standard regulations.

5 However, again, we are not in favor of making
6 these changes across the board. We're looking at it
7 industry by industry. I believe if you change the size
8 standard industry by industry, you are not going to have
9 the same effect that you're looking at with the 34,000
10 small businesses that would no longer be small. I think
11 you would find a much, much smaller amount if you do it
12 industry by industry.

13 Those are all my comments. Thank you for your
14 time. Do you have any questions?

15 MR. KLEIN: The annual or two-year
16 recertification that you were talking about, were you
17 talking about payroll tax contracts only? I'm not --

18 MS. GUADARRAMA: Actually I'm talking on both
19 of them, whether or not you're a small business that has
20 to be recertified or whether you currently have a
21 contract.

22 If you specifically look at the GSA contracts
23 that are out there that are originally like four or five
24 years and have four options to it, that actually makes
25 it a 20-year contract. I'm completely against saying

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1 that you're a small business when you're affecting your
2 small business for those 20 years. That's putting small
3 businesses at a horrendous disadvantage.

4 MR. KLEIN: Now, what about the general small
5 business contracts that someone gets as a small business
6 and grows over a five-year period? Do you feel that
7 they should get --

8 MS. GUADARRAMA: We're still saying one or
9 two-year recertification for --

10 MR. KLEIN: So for their options, in theory,
11 they could be other than small in their options under
12 that contract as well?

13 MS. GUADARRAMA: Most of the contracts that are
14 out there, you can continue with that contract even if
15 you're not a small business. It is simply no longer
16 being credited under the small business program. So I
17 think that clarification needs to be made. Some people
18 are concerned that they no longer get to continue
19 working with the contract. Contract is in place. You
20 still send out a contract, but it cannot be used as
21 small business credit.

22 MR. KLEIN: Another point you said, you said
23 something about there are firms out there that are
24 dominant in their field today. Are you talking
25 geographically or nationally? What do you see?

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1 MS. GUADARRAMA: Dominant in the field in terms
2 of you've got a number of businesses that are still
3 considered small businesses that are dominating the
4 field nationally --

5 MR. KLEIN: You mean nationally?

6 MS. GUADARRAMA: Yes.

7 MR. KLEIN: I was trying to understand what you
8 were saying.

9 MR. JACKSON: I just wanted to ask you a
10 question on the tiering, if you oppose that concept.

11 We have had some testimony -- you may have
12 heard some of it in San Francisco -- but in other
13 hearings and comments that we got from the advance
14 notice spelled out a three to five-year or five-tier
15 system where certain categories of small businesses
16 would compete for certain contracts. So very small
17 businesses, however defined, would be able to compete
18 for certain contracts, and then larger small
19 businesses -- and some have proposed as high as 1,500 --
20 could compete on much larger contracts, but all small
21 businesses would compete for those types of contracts.

22 Do you think that that system is workable?
23 Again, I know you oppose it. But if it were structured
24 in a way that certain segments of small businesses could
25 compete for certain contracts, again, do you feel that

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1 that has any viability within the federal market?

2 MS. GUADARRAMA: No. When we look at small
3 business size standards, I think that the first question
4 that you all have under the proposal is are they
5 currently difficult to understand.

6 I think for the most part they are not. When

7 you start putting a five-tier program together, and
8 under those five tiers, small businesses can now only
9 work with a small business set-aside that's specifically
10 in that tier that's been set aside for that size, I
11 think you're looking at something very complicated.

12 I think as it is, we have lot of procurement
13 folks out there that are not really clear on how to work
14 with the size standards to begin with. Now we're going
15 to put a five-tier program out there and say, "In this
16 area I get to be part of that tier that's 50 to 100. In
17 this one, I'm part of the 100 to 150, but I'm excluded
18 from the other one because I've gotten bigger."

19 I think just hearing the explanation of it is
20 completely confusing, much less trying to put it in
21 operation. We're completely against it.

22 MR. JACKSON: I heard it twice. Four times.

23 Another question. I apologize for the audience
24 because this is probably the only hearing, and we've had
25 ten people talk, and our SBIR issue has not come up in

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1 much substance.

2 But I know that yesterday when we were in
3 San Francisco, we heard a number of biotech companies
4 testify that they are small firms. One had 20
5 employees. One had 80. They were around that size. So
6 they felt that they were small businesses.

7 But they also felt that within their industry,
8 to be able to commercialize their R and D, which they
9 indicated would take a minimum of \$800 million over a
10 ten-year period before they could commercialize that
11 product, that they needed significant venture capital
12 resources, and generally that would result in companies
13 being majority owned by either a single, but in most
14 cases multiple, venture capital companies.

15 From the comments that you heard along those
16 lines, did you see anything in their argument that you
17 thought was persuasive, or do you feel that that 49
18 percent limit is a good cutoff?

19 Again, any observation on their arguments that
20 you would like to share?

21 MS. GUADARRAMA: I still think that the
22 49 percent is a good cutoff. I just find it hard to
23 believe that the venture capitalists are interested in
24 the company if they can own 51 percent, but if they can
25 only work with 49 percent, that they're not going to be

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1 funding them.

2 I think that one of the gentleman in particular
3 was talking about his company, and someone from the SBA
4 specifically asked him to describe what the management
5 of his company now looked like with the vent capitalist
6 that he had working with him.

7 And he had said originally that there were
8 three individuals who founded the company. They now
9 have two left, the two of them working R and D. The
10 VCCs were the president, they were the CFO and the COO.

11 Now, I find it hard to believe that with VCCs
12 being the president, the CFO and the COO, that that's
13 still a small business simply because two of the
14 founders are still doing R and D.

15 And as soon as he said that, my impression is
16 he now works for the VCC company. You know, whether or
17 not they call themselves founders, in reality they have

18 no control over it anymore

19 MR. ALVARADO: Let me, if I might, take you up
20 on this -- even though I think I know better than to do
21 that -- the same question that I asked Ms. Hazel and if
22 you will remember the admonition to be gentle.

23 Life after the 8(a) program -- care to comment
24 about that?

25 MS. GUADARRAMA: Absolutely. We graduated from
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1 the 8(a) program probably about four years ago. It has
2 not had a detrimental effect at all on the record of the
3 company.

4 In our case, probably one of the reasons is
5 that the entire time that we were in the 8(a) program,
6 we made sure that we had more than probably at the most
7 50 percent of our portfolio in 8(a) contracts to make
8 sure we were balanced at all times. And as we got
9 towards the end of the 8(a) program, we made sure we had
10 less and less reliance on any type of 8(a) contracts.

11 However, when you graduate, what used to be in
12 effect -- when you graduate from the 8(a) program, you
13 are automatically certified for three years as an SBA
14 company, as a small disadvantaged business.

15 Before -- I think it was under the Clinton
16 administration that they looked at the SDB program and
17 decided that a moratorium needed to put be on the
18 program.

19 You used to have SDB set-asides; so when you
20 graduated from the 8(a) program and you still had three
21 years as a certified SDB, you had a completely separate
22 program that you could then start working with, which
23 was SDB set-asides. So that took you from the 8(a)
24 program, SDB set-aside program, into that small
25 business.

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1 When the moratorium was put in place, it was a
2 three-year moratorium on the SDB program. That was
3 seven years ago. The moratorium is still in place
4 although generally, when there's a moratorium, it means
5 after that three-year period, it's lifting the program
6 back in place.

7 The program has not been cancelled. It's still
8 there. It's simply, for whatever reason, we're still
9 operating as though the moratorium is in effect. I
10 think the SDB set-aside program was a great vehicle for
11 8(a) companies, when they graduated, to still have a
12 another program to work with before they just went
13 straight into a small business program.

14 MR. ALVARADO: So you would advocate something,
15 some --

16 MS. GUADARRAMA: I would advocate bringing back
17 the SDB set-aside program. It's still there. It
18 doesn't take legal maneuvering to actually get it back
19 in place. The moratorium has expired, and my
20 understanding is if the moratorium expires, the program
21 is available for use again.

22 MR. KLEIN: Actually, the SDB for civilian
23 agencies expired last September for set-asides as well
24 the price evaluation preference. It's still in effect
25 in theory for the DOD agencies. However, the price

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1 evaluation adjustment is not available for DOD agencies.
2 Because if you were meeting your goals from the previous

year, you will not be able to use the price evaluation preference in the next year. And they have been meeting the goals. So SDBs -- even if the evaluation preference is not available for them as well as the set-asides, again, the DOD moratorium has expired presently. There is talk about revising it, but we have not seen that.

MS. GUADARRAMA: Well, since the DOD is probably the largest federal agency that we have with dollars actually spent on small businesses, the fact that they could be using SDB set-asides, I think that's something the SBA should be taking a look at.

MR. KLEIN: Thank you very much.

MS. GUADARRAMA: Thank you.

MR. KLEIN: Let's have a quick break. Ten minutes. Thank you.

(Recess 10:33 to 10:50.)

MR. KLEIN: Charles Bull.

MR. BULL: My name is Charles Bull, B-u-l-l. I'm the president of RECON Environmental. We're located at 1927 Fifth Avenue in San Diego.

RECON is a small business with average annual sales of about \$7 million, and we have 120 employees. We provide a full range of environmental services,

including NEPA compliance, air and noise modeling and conservation planning. We also have a native plant nursery and have an extensive field restoration program.

We're a HUB-zoned status business and have received a lot of benefit from the Small Business Administration's effort to promote small businesses and the federal government's focus on expanding these opportunities.

I've come here today to address several points on your proposed rulemaking regarding small business size standards, but I want to limit my remarks to four points raised in the proposed rules.

Two of them, calculating the number of employees and the use of receipt-based size standards, are really integral for us, and they're inexorably intertwined.

Our primary NAICS code has a size standard currently of \$12 million. With the proposed change in the size standards, we become a large business by the definition because the standard is now set at 100 employees.

The reason this happens for our primary NAICS code is that the economic census calculated an average receipt of \$118,000 per employee and applied that receipt to the size standard of \$12 million.

RECON's average receipts per employee is \$60,000, about half of what the census data provided. This results from the fact that a substantial portion of our staff is in the field and bill at a really low rate, resulting in a very low per-employee cost.

To put this in perspective, based on the services that we provide, if we're classified as a large business because of the number of employees, we're now competing with SAIC, CH2M Hill, URS, who have receipts of between 8 billion and \$3 billion and staffs between 42,000 and 14,000 employees. Their per-employee sales are between 122,000 and \$190,000 a year compared to ours of \$60,000 a year. Each of these obviously have

significant competitive advantages over us from our size.

If you want to use the number of employees, then some measure, I think, needs to be taken into consideration for firms like RECON that employ a substantial proportion of their staff in low-billing-rates positions.

Of course, adjusting the number of employees based on a firm's average per-person sales is simply a receipt-based size standard.

Clearly, we feel that you should retain a receipt-based size standard to classify small

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businesses. You've done this for construction. They obviously have a lot of materials costs and things. And we propose that you do it for us as well.

Next issue is the designation of the size standard for the procurement. This is probably the most contentious issue of a business our size. There really is no NAICS code that specifically addresses our range of services.

Contracts that we may wish to bid on are classified anywhere from \$2 million as a size standard to 500 employees. For the process that contracting officers use to designate the code for a specific procurement for us is somewhat obscure. Similar projects do not always use similar codes. Different agencies apply them in different ways. Some mechanism is needed to provide consistency across solicitations and agencies.

I have sort of an off-the-wall idea, and we'll just sort of chalk it up to the fact that in a small business we're trying to be innovative. But in recognizing that a firm might be considered small under one code and large under another and further understanding the difficulty a contracting officer faces in assigning a specific code, we suggest that the government not assign a code to a particular project,

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but rather indicate, when a response is made to a request for a project that is a small business set-aside, the firm applying to that request submit their code as part of the application.

The contracting agency could therefore select the most qualified small business without being constrained by specific standards. The only criticism I can see to this approach is that different sized firms could be considered for the same job, both receiving different small business standards. This could be avoided by selecting the smallest, best-qualified firm from the applicants.

Finally, grandfathering. The proposed rules mention that while changes will invariably have an adverse impact on a few small businesses, the suggestion is that an implementation period longer than 30 days might allow those businesses to adjust to the new regulations.

Because after the adoption of the rule we will be 20 percent over the proposed employee standard while the day before we were 42 percent below the standard and because after the adoption we will lose our HUB-zone status, we are one of those firms that will invariably be impacted by the proposed rule.

25 This impact can clearly be avoided by allowing
00093 1 a firm to maintain its existing status until they
2 outgrow the requirements on the standards as amended in
3 August of 2003.

4 Thanks very much for your time.

5 MR. KLEIN: Regarding grandfathering, how long
6 would you --

7 MR. BULL: I would grandfather a firm in as
8 long as they met the standards under which they
9 originally were established as a small business.

10 MR. KLEIN: Now, in terms of -- you said
11 similar projects don't use similar codes at times.

12 Do you believe that the size standards for
13 similar types of work should be similar so that code
14 shopping would not be done?

15 MR. BULL: If there was a mechanism to
16 objectively apply a code to a particular type of work,
17 then I would think that would be appropriate. But I
18 oftentimes think that the assignment to a particular
19 code is arbitrary or left to the judgment of the
20 particular officer who's establishing the contract.

21 MR. KLEIN: But if it's two codes that could be
22 used in the same size standard, it wouldn't matter?

23 MR. BULL: It wouldn't matter.

24 MR. KLEIN: So would you propose similar type
25 work having the same size standard, or would you think

00094 1 the way -- for example, environmental remediation has
2 some very big codes. Sometimes that type of work is
3 called engineering. Sometimes it's called construction.
4 Each of those have very different types of size
5 standards.

6 Does it make sense for them to have separate
7 size standards, or should they be similar size
8 standards?

9 MR. BULL: I think that when you set size
10 standards, it needs to be set for the type of business
11 that's involved.

12 Obviously, a construction firm has a different
13 requirement from a sales standpoint if you're doing it
14 based on receipts, which we think you should do, than
15 would an engineering firm. So I'm not sure I understand
16 the question completely.

17 MR. JACKSON: I just want to follow up with a
18 few more questions about the NAICS code selection.

19 In your experience where you see the variety,
20 are the contracts significantly different, or do you
21 view them as very similar requirements?

22 MR. BULL: The problem that a firm like ours
23 faces is there is really no code that covers the range
24 of services specifically that we provide. There are
25 several codes that do things that we do provide, and

00095 1 there are a lot of firms that are in our same situation.
2 So size standards get applied differently to
3 different contracts because of picking -- you know, if
4 you look at the description of the codes, they don't
5 match the work that's being proposed. So that's where
6 the complication comes in.

7 MR. JACKSON: Again, your competitors are in
8 the similar situation and offering basically the same
9 type of services --

10 MR. BULL: Absolutely.
11 MR. JACKSON: -- that you offer?
12 Thank you.
13 MR. KLEIN: Thank you very much.
14 Terry Bibbens.
15 MR. BIBBENS: Good morning. My name is Terry
16 Bibbens, B-i-b-b-e-n-s. I'm managing director of
17 Homeland Venture Partners with offices in L.A., Irvine,
18 Silicon Valley, and San Diego.
19 I want to express my appreciation to
20 Mr. Jackson and the team from D.C. for doing this round
21 robin. I know it's been a very long process, and we
22 appreciate your outreach across the country here. And
23 I'm delighted that one of our offices is in the best and
24 biggest districts here and that all of our offices are
25 in the best and biggest region.

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1 I'm going to be brief because you have many
2 others here today, and I'm going to focus only on one
3 issue. And I've provided a hard copy and floppy of the
4 testimony I'm going to be reading today.
5 I'm going to focus on NO. 11, specifically the
6 VC-majority-owned companies being involved in the SBIR
7 company.
8 I'm a managing director of Homeland Venture
9 Partners, a 100 million fund in formation. I'm flatly
10 opposed to any business that is majority owned by
11 venture capital being permitted to participate in the
12 SBIR program. And I'll repeat. I'm flatly opposed to
13 majority-owned VC companies being able to participate in
14 the SBIR program.
15 I'm frankly quite frustrated by the proponents
16 of those who advocate this. They've tried to paint
17 their story as valuable to the U.S. taxpayers, to the
18 agencies, and to the small SBIR companies.
19 In my opinion, nothing could be further from
20 the truth. No matter how they dress that pig in fancy
21 clothes, it is still a pig. And I use that metaphor
22 with intent.
23 The wealthy VC leaders pushing this proposal
24 see some of the value that Congress has built into the
25 SBIR program to permit the data rights to accrue to the

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1 small SBIR companies for many years after patents would
2 normally run out.
3 Congress put these data rights into the SBIR
4 program to encourage small companies to commercialize
5 their advanced technologies. The SBIR data rights can
6 essentially go on forever; that is, it's four years
7 after the last delivery of the last item on a government
8 or commercial contract versus the typical 20 years of a
9 patent term.
10 To the bio and life sciences companies, being
11 able to control the data rights essentially forever and
12 eliminate the opportunity for patent drugs to become
13 generic is a dream come true. Unfortunately, this comes
14 at the expense of the SBIR program and the public users
15 of these products.
16 GAO and the Academy of Sciences has studied
17 this program, the SBIR program, many, many times, and
18 they found it to be the most effective R and D program
19 in the world. And that's been studied again 13 times by
20 GAO.

21 And they found that the quality of the research
22 is second to none, including that by large businesses,
23 universities, and the federal laboratories.

24 One of the reasons it's effective is it permits
25 scientists in tiny companies, even researchers from

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1 academia who are just starting a company -- they can bid
2 on a program, an SBIR program, because they have
3 typically a 25-page limit to the proposal. You don't
4 have big overhead costs for submitting proposals.

5 As a founder of Homeland Venture Partners,
6 focused primarily on SBIR companies in the defense and
7 security business, I believe that permitting
8 VC-controlled companies to compete in the SBIR business
9 would accrue benefits only to the VCs.

10 And here's why I believe that: In order to
11 receive funding from a VC firm, a company has to have a
12 maturity of organization that only a few of the SBIR
13 companies have. The previous speaker spoke to that
14 comment about the company that only had two of the
15 founders left in management roles.

16 Second, with the millions of dollars invested
17 by the VCs in these companies, these now large companies
18 would be able to prepare proposals and provide equipment
19 for the research work that large companies would
20 typically have.

21 Third, this will squeeze out some of the best
22 and brightest scientists and innovators from the small
23 companies.

24 Fourth, the VCs will be focused only on those
25 life science projects that have large potential dollar

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1 returns, not on the fundamental science which the SBIR
2 program performs so well in. General partners of a VC
3 firm, like me, need to provide liquid returns within ten
4 years. That's not what the SBIR program is about in
5 fundamental research.

6 I will finish up on my pig metaphor. The
7 average salary of a GP of a large VC fund, much larger
8 than ours, is on the order of 2 to 3 million a year.
9 That's the salary of the management fee. Their partner
10 carry is on the order of \$5 million.

11 So over a ten-year period, you have between 5
12 and \$8 million per year to that GP. They do not need
13 the small amounts of money that the SBIR program has to
14 succeed.

15 Thank you very much for your time.

16 MR. JACKSON: Mr. Bibbens, at some of the other
17 hearings that we have attended, we've heard testimony
18 mainly from the biotech industry that there's not
19 alternative sources of R and D for proof of concept, and
20 the VC investment is directed more to commercialization
21 of a particular product.

22 Do you agree that there are not viable funding
23 sources for that other type of proof of concept
24 research, or is that misleading?

25 MR. BIBBENS: If I understood your question

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1 correctly, I believe that that's quite misleading. The
2 VCs -- I've got some data I've provided as a backup
3 here -- the VCs typically are getting out of the seed
4 and start-up phase. The charts keep going down. In the
5 seed and start-up phase, I think the numbers -- the

6 first quarter of 2005, there were 171 companies funded
7 in the seed and start-up face.

8 The government R and D is very robust in the
9 SBIR kinds of programs. We have something like 8,000
10 SBIR programs a year. And the 100,000 and above and the
11 750 to a million dollars are very appropriate to
12 continue feeding the commercialization programs.

13 MR. JACKSON: Just a follow-up question. You
14 alluded in your testimony about the purpose of the
15 program.

16 If SBA made a change that would allow
17 majority-owned companies -- majority owned by VCs -- to
18 participate in the program, regardless of how it's
19 defined but just in general, what do you think the
20 impact on existing businesses that participate in the
21 program would be?

22 would it crowd out opportunities, or would it
23 have a geographical displacement to any significant
24 degree?

25 MR. BIBBENS: Yes, let me speak to the last

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1 part first.

2 The geography -- the data -- and I've got this
3 in the attachment here -- California receives 46 percent
4 of the total venture capital in the United States. 79
5 percent of the total venture capital in the United
6 States going into companies in the states are in
7 California, New England, New York, Pennsylvania, the
8 D.C. metroplex, and Texas.

9 Now, what this would do would permit that
10 concentration to be reinforced in the SBIR program.
11 where we know that the brilliance is not concentrated in
12 Silicon Valley, it's -- that's the funding, the venture
13 capital funding, is concentrated there.

14 So I think this would be quite detrimental
15 geographically in other than those five or six states.

16 Your first question -- I think that the SBIR
17 program again covers a wide spectrum of technologies
18 from the very basic research at NIH and at the National
19 Science Foundation towards more applied things for the
20 Department of Defense and others who are looking to use
21 the technology for the fighting forces and so forth.

22 Again, I believe there's very robust funding
23 available in the SBIR program and other federal
24 programs. And those companies who have a good
25 commercial product potential will be able to get the

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1 venture capital. That's what we're set up to do, and we
2 see a robust market out there.

3 But I will reconfirm: We never plan to have
4 majority ownership of any of our companies. We think
5 that's bad for the company. We think we should be
6 investors.

7 And the concern of the biotech companies
8 talking about \$800 million to go through an FDA, that's
9 an absolutely true statement. But they are no longer a
10 technology company appropriate for the SBIR. By then
11 they're into manufacturing controls, FDA compliance for
12 quality, compliance for labs and for manufacturing.
13 That's completely inappropriate for the SBIR program.

14 MR. JACKSON: Thank you.

15 MR. MANALISAY: Mr. Bibbens, just to follow on
16 to that answer, then.

I just picked up on what you said in the commercial market that if there's a commercialization for the technology, then there's a very robust funding.

Does that necessarily -- are you saying necessarily, then, that if there is not necessarily a commercial market available, that firms may see some difficulty in finding funding for them?

MR. BIBBENS: The answer is yes, they will always find difficulty getting funding if there's no

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market to commercialize it into because the investors see no return. That would be true whether the VC owned 50 percent or not. They would curtail the \$800 million investment to go through phase 3 clinical trials if they saw there wasn't a market for it.

MR. MANALISAY: Even if there is an SBIR topic in that area, knowing the firm, it sees that there's work out there, but it's not necessarily commercialization?

MR. BIBBENS: I think the best way to address that is there are many SBIR topics and many research topics in all of our agencies outside of the SBIR. And again, the SBIR only covers 2.5 percent of our total federal research 6162 monies.

There are many topics in which we need to push the state of the art in which commercialization may come two or three other programs later. Nanotechnology is an area -- microlithography, other areas where it takes decades to make the kind of progress before you get a commercializable program.

That has nothing to do with the biotech industry trying to get VC-majority owned companies back into the SBIR. In my opinion, it's as wrong as -- as many other speakers we've had this morning -- of having a small company have to compete against a Lockheed and

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others.

And I'm afraid this proposal would -- should it go through. I know it's not your proposal. It came from industry. If it should go through, it would make it very easy for large firms to set up their own VC firm -- and many have them -- and then set up their own companies. And they would comply, and it would be a big pharma or a big company. That's completely inappropriate for everything that the SBA and the SBIR program stand for.

Thank you very much.

MR. KLEIN: Ivor Frischknecht.

MS. BAILEY: I'm April, but I'm not Ivor.

April Bailey, B-a-i-l-e-y. Good morning. My name is April Bailey, and I'm here representing BIOCOM. We're the regional association for Southern California's life science industry.

BIOCOM greatly appreciates the opportunity to testify on this very important issue, and I would like to thank the SBA and members of the hearing panel for conducting these hearings.

BIOCOM has a diverse membership consisting of approximately 400 member companies working in various sectors of the life science industry, including biotechnology, biopharmaceuticals, medical devices and

00105

diagnostics as well as academic and research

2 institution.

3 we have companies ranging in size from three
4 employees up to thousands of employees. Pfizer is a
5 member of ours. I don't think Pfizer really cares about
6 this issue today, but Pfizer is a member of ours. So we
7 have a huge range of members.

8 Because of the nature of operating a trade
9 association, we must insure that we are representing the
10 best interests of our member companies and are
11 representing the vast majority of our membership.

12 BIOCOM has taken several informal polls between
13 2002 and 2005, and more than 90 percent of our member
14 companies agree with the position that we will be taking
15 today.

16 It our understanding that this hearing is being
17 held to seek input on whether the SBA should disregard
18 its affiliation rules for SBIR program purposes and
19 allow business concerns that are majority owned by a
20 venture capital company or multiple venture capital
21 companies to be eligible for SBIR awards regardless of
22 any affiliations arising from the ownership or interest
23 of the VCC.

24 We strongly believe that the exclusions that
25 will result from an interpretation of eligibility

00106

1 requirements that define "individual" as a natural being
2 and not an entity are not in the best interest of the
3 program, the industry, or in line with congressional
4 intent.

5 Our membership has a great interest in the
6 eligibility requirements as they have long been
7 participants in the SBIR grant program. California is a
8 magnet for both venture capital and public grant
9 funding.

10 California's emergence as home to two of the
11 three largest life science clusters in the United States
12 is in large part due to the strong research base and its
13 ability to attract funding for scientific research. The
14 success of the industry is a testament to the fact that
15 the program, as written by Congress, is working as
16 intended.

17 Another major concern that arises from the
18 change in eligibility requirements, or proposed
19 eligibility requirements, is how it could affect the
20 ability for the best science to be funded.

21 The agencies that fund the SBIR program and
22 evaluate the grant proposals have an interest in seeing
23 the most qualified proposals funded. Making the
24 eligibility standard so narrow disqualifies the
25 companies who have had their technology validated

00107

1 through the attraction of investors.

2 In doing so, it forces the funding of the
3 second-tier scientific research which undoubtedly is in
4 conflict with congressional intent of maintaining the
5 United State's dominance in scientific research.

6 We also believe that interpretation of
7 "individual" as a natural person is adverse to the other
8 stated intent of Congress when passing this legislation,
9 which is referenced in the legislation as to "attract
10 private capital to commercialize the result of federal
11 research."

12 It is obvious that the Congress, when passing

13 this legislation, had an understanding of the business
14 model associated with the biotechnology industry. A
15 diverse portfolio of investment that includes a
16 combination of venture capital, angel investors,
17 personal investment, private partnerships, public
18 offerings, and grants is critical for small companies to
19 meet all the financial challenges they face in taking
20 new and innovative technologies from the laboratories to
21 commercialized products.

22 It is not clear whether the current leadership
23 in the SBA, who is seeking to reinterpret the criteria,
24 have the same understanding or are in agreement with
25 congressional intent.

00108

1 To solve the problem that has been created by
2 the reinterpretation, we urge the SBA to clarify
3 eligibility requirements through a proposed rule that
4 reflects congressional intent.

5 We recommend that the SBA adopt a rule that
6 addresses the realistic model of companies working in
7 this industry who have attracted private investment in
8 the form of venture capital. In doing so, a revision
9 must be made to permit VCC ownership of SBIR applicants
10 to account towards the 51 percent U.S. ownership and
11 control requirement.

12 This would allow better quality and increased
13 quantity of applications to be reviewed for the purpose
14 of grant making but would still exclude corporate
15 interests and their affiliates from unduly using this
16 program.

17 Thank you for your time. Questions?

18 MR. JACKSON: Just a couple questions.

19 We've heard testimony previously just right
20 before and after the break taking an opposite view. And
21 I notice two themes in those testimonies. One relates
22 to the purpose of SBIR programs and the other more of a
23 public perception. So I want to ask questions somewhat
24 along those two lines.

25
00109

1 Why is there a need for VCs to have more than
2 49 percent investment in these companies? That VCs can
3 invest in companies eligible for the program, but under
4 current regs, if it's more than 49 percent, it's then
5 considered an affiliate.

6 Why is there a compelling need to consider
7 going beyond that threshold?

8 MS. BAILEY: Well, a lot of times with a
9 biotechnology company, venture capitalists, while they
10 do look at the management structure of a company,
11 they're actually investing in research. So if a company
12 has two or three compounds or molecules that they are
13 working on at one time, quite often a VC will express
14 interest in a certain compound, and they will want to
15 fund the research for a certain project.

16 So it would be more project based than company
17 based. So then, if you have two, three, four VCs that
18 are all looking at different compounds or projects that
19 they want to have funding in, then you get more than
20 51 percent by the nature of that.

21 There are also companies that have very
22 aggressive research goals and require very significant
23 influxes of cash. And when that does happen, then they
-- you know, to be honest, some companies sell their

24 souls, so to speak, and allow some unfavorable terms on
25 their funding.

00110

1 what's interesting about that is we did do a
2 poll of our companies in 2003, November of 2003, to find
3 out if any companies that had been formed and had
4 received this venture capital funding of 51 percent were
5 actually run by the VC. And we found one company in
6 San Diego that did have that happen, where the VC did
7 come in and take over management.

8 It should be noted that that VC was the founder
9 of Hybertech, which was the first biotechnology company
10 in the state of California. This VC has also run 14
11 other biotechnology companies before becoming a VC. And
12 he decided, not because he was a VC but because he had
13 been intricately involved in that company, prior to even
14 funding that company, on a research basis, that it would
15 be in the best interest of the company for the
16 management to leave.

17 So that is not something that is common. We
18 have one case where that's actually happened, they've
19 actually come in and taken over.

20 MR. JACKSON: How do you prevent control? How
21 can you have majority ownership and not have control?

22 MS. BAILEY: It's usually done through the
23 actual agreements of the venture capital -- the
24 agreements that happen. There are licensing agreements
25 in addition to -- when you go in, they get a certain

00111

1 percentage. A lot of them have exit strategies, as
2 Mr. Bibbens did speak to, that they want to get out
3 within ten years.

4 Most of them do not include an option to take
5 over the company. The only way that they would be able
6 to take over the company is not only their 51 percent
7 but if the board of directors actually also decided that
8 the management was unfit.

9 We have had companies where it was decided that
10 the management was unfit and the management was
11 dismissed, basically. But it's not usually instigated
12 by the venture capitalist. I can't even think of one
13 case where it has been instigated by the venture
14 capitalist.

15 MR. JACKSON: Thank you. Getting to the second
16 theme again, there was testimony here where the public
17 perception of a group of well-financed VCs benefiting
18 from a program that's targeted to small business R and D
19 firms.

20 Can you comment on that? Again, there is a
21 perception out there that who is really benefiting, the
22 VC or the small business?

23 MS. BAILEY: I completely understand that
24 perception. I think where the perception needs to be --
25 or where the discussion needs to head to is it's not the

00112

1 VCs that are usually benefiting from the programs. It's
2 the companies that are benefiting from the SBIR program.

3 We have two companies right now that are
4 actually working in the area of homeland defense who are
5 in great fear of having their SBIR grant being taken
6 back. And the reason is that they -- they did submit
7 for a specific grant. They were found eligible on every
8 criteria.

9 However, while doing that, there's another
10 compound that they are also pursuing. And there's a VC
11 that wants to come in and aggressively fund that
12 compound because they do believe there's a commercial
13 applicability.

14 So what does this company do where they're
15 trying to -- in this case, it's actually a vaccine for
16 avian flu. And so they're trying to work on this, which
17 they've already answered the grant proposal and they've
18 actually already been awarded. But they have other
19 business opportunities as well.

20 So I think it's the companies, not the VCs,
21 that are necessarily benefiting from this.

22 MR. KLEIN: Thank you. Number 13.

23 MR. FRISCHKNECHT: So I am Ivor Frischknecht.
24 I'm Ivor Frischknecht. That's spelled I-v-o-r,
25 F-r-i-s-c-h-k-n-e-c-h-t. I'm a director at Idealab,

00113

1 which is a small local private firm.

2 Even though I'm representing Idealab here and
3 I'm going to address comments specifically to our
4 issues, I can also speak to this venture capital
5 partnership issue more generally, if you'd like,
6 afterwards.

7 We strongly support a change in the size
8 standard, particularly with respect to technology
9 start-ups so that the size standard reflects that that
10 is in the SBIA legislation for enterprise SBICs, small
11 business investment corporations.

12 Idealab is a small private company that creates
13 and helps build pioneering technology companies. Since
14 1996 our companies have created thousands of jobs, and
15 Idealab has provided hundreds of millions of dollars of
16 funding for them.

17 The way it works is that once a promising idea
18 has been identified, it is incorporated into a separate
19 operating company. And that operating company is funded
20 and housed by Idealab.

21 Once a company has the founding staff -- and
22 these often come from outside -- these founders will
23 hire the rest of the team. If the company prospers, it
24 will graduate from our offices, or incubator, and find
25 its own premises.

00114

1 What I have described is a typical technology
2 start-up. Indeed, the companies that Idealab builds are
3 the same as any other small technology start-ups in all
4 respects except that Idealab typically holds a majority
5 of the equity of each company from its inception.

6 This reflects the fact that Idealab is taking a
7 very large risk by investing its resource and capital at
8 a very, very early stage. It seems exactly this kind of
9 new technology-oriented risk taking that the SBIR should
10 be encouraging.

11 Our companies are involved in various
12 ground-breaking research and product development in
13 robotic vision, large database analysis, solar energy
14 generation, efficient external combustion engines, and
15 optical wireless communications.

16 All these areas -- and there are others -- but
17 all of these particular areas have been identified by
18 the U.S. government as priority areas worthy of public
19 funding.

In fact, some of our companies have been approached by government officials to encourage them to apply for particular SBIR and STTR opportunities. Due to the current rules, they're unable to do so, and it's the 51 percent ownership that they run into.

The consequence of this is that the new

initiatives that the government has identified are relatively underfunded and not as developed as they would be if there were access to this funding.

In fact, one of our companies has been in conversation with DARPA and other military branches to develop battlefield technologies. The contracting offices suggested SBIR and STTR funds, but because they were not available to the companies, the two parties will be going through the normal contracting process. This means a 6 to 18-month delay for funding and with potential risk to the battlefield troops.

The reason Idealab is not eligible for SBIR funding is that many of our operating companies are counted in the definition of "affiliate." The total employee count of Idealab with all these affiliated companies is over 500.

We believe that Idealab qualifies as a venture capital operating company as defined by the U.S. Department of Labor regulations.

There are specific solutions to our company's problems in having access to these funds -- and I should emphasize they start usually with 2 people and then grow to about 50 people before they graduate from the incubator -- so at all times, small business in the way one would commonly see it.

In the case of SBIR, removing other like start-up companies -- such as, for example, our operating companies -- from the definition of "affiliate" or removing Idealab -- namely, the venture capital type entity -- from the definition of "affiliate" would accomplish the goal that we're after.

A specific way to do this would simply be to bring the definition in line with the SBIC definition, small business investment corporation.

We believe the same change should be made in the case of the STTR program. We weren't able to come up with any logical reason as to why the size requirements should differ between STTR, SBIR, and SBIC, and submit that whatever definition is settled upon, it should apply equally to all three programs.

We believe that venture-funded start-ups are more likely to succeed than those that are not, and we count ourselves in that category. Hence, it is a more efficient use of public funds to invest in such companies.

It is a way for public agencies to make full use of the private sector's diligence. Usually investors will spend a month or more deciding what to invest in. The current rules paradoxically enforce a contrary funding approach by the government: whatever

technologies and businesses the private sector believes are most to succeed and, hence, are more than 50 percent owned, are the ones that the public sector won't fund.

Thank you.

5 MR. JACKSON: Just a quick question.

6 Under the final rule that we published last
7 December that went into effect in January, if the parent
8 company would be an otherwise eligible company, meaning
9 51 percent owned by individuals, not -- I know that your
10 company is over 500 employees, but if your company was
11 under 500 employees, would you qualify -- or would the
12 companies that you own qualify for the program?

13 MR. FRISCHKNECHT: Yes. So Idealab is more
14 than 50 percent or 51 percent owned by individuals. So
15 that is not an issue.

16 The issue is that -- and Idealab itself is a
17 small company. There are something like 70 employees.
18 But it's because all the other start-up companies that
19 we have created, some of which are successful, happily,
20 are counted in the "affiliate" definition, that none of
21 our companies are eligible for the funding.

22 MR. JACKSON: Just for clarification for the
23 audience, the size standard for the SBIC, small business
24 investment company program, is net worth and net
25 income -- \$6 million in net income in and, if my memory

00118

1 is good, 21 million in net worth.

2 Again, there are different measures, and a firm
3 can qualify under the general small business industry
4 standards or net worth/net income standards.

5 \$18 million.

6 MR. FRISCHKNECHT: Yeah, there's a specific
7 exception for venture capital as operating companies, as
8 owners.

9 MR. JACKSON: Okay. Again, our final rule
10 could benefit you if you were under 500 employees, but
11 because it isn't, looking at a different size standard
12 requirement would be your preference to address your
13 situation?

14 MR. FRISCHKNECHT: Right. Or simply a change
15 in the "affiliate" definition to make it slightly more
16 narrow.

17 MR. JACKSON: Okay. Thank you.

18 MR. FRISCHKNECHT: Thank you.

19 MR. KLEIN: We'll go with Melissa Yamaguchi.

20 MS. YAMAGUCHI: Good afternoon. My name is
21 Melissa Yamaguchi, Y-a-m-a-g-u-c-h-i. And I'm here
22 today before you representing -- I'm the president of
23 the Professional Beauty Association. We represent
24 60,000 employee-based professional salons and spas in
25 North America that have 80 percent female ownership.

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1 I'm also the owner with my husband of five
2 salons here in Southern California. Thank you for the
3 opportunity to comment on the issues presented in the
4 SBA Advance Notice of Public Rulemaking on Small
5 Business Size Standards.

6 As an industry that is primarily comprised of
7 small independent businesses, it's extremely important
8 for the salon industry to remain and to maintain the
9 existing level of eligibility for SBA programs and
10 assistance.

11 In its Advance Notice of Public Rulemaking, the
12 SBA stated that it proposed to restructure its size
13 standards as a way to simplify and make them easier to
14 use.

15 while the application of size standards may be

confusing for businesses in some industries, this has not been a problem in the salon industry. The current receipts-based size standards of \$6 million in annual sales is extremely user friendly and easy to apply.

As such, I believe that the current system of size standards would preserve the existing simplicity from the perspective of small businesses in my industry. In the proposed restructuring of size standards issued on March 19, 2004, the SBA established a 50-employee size standard for nonmanufacturing industries with the

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current \$6 million size standard. This size standard was referred to as the nonmanufacturing anchor size standard.

Unless other criteria are present within an industry, this nonmanufacturing anchor size standard was applied to all nonmanufacturing industries with the \$6 million size standard.

A defining characteristic of our salon industry is the fact that it's extremely labor intensive with its employees generating a relatively small amount of sales compared to most other sectors of the economy. According to data from the census bureau, the average receipts-per-employee ratio in the salon industry is less than 40,000 per employee.

As a result, I believe that it is very important for the salon industry to be considered separately from other nonmanufacturing sectors if the SBA chooses to move forward with the restructuring of size standards.

In its ANPRM, the SBA requested comment on a number of issues, including the calculation of the number of employees for size standard purposes.

While I strongly believe that the current receipt-based system of size standards is appropriate for our industry, I would have several concerns about

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the method in which SBA calculates the number of employees for a business if, in fact, the SBA chose to change from a receipts-based size standard to an employee-based size standard.

In particular, the method of calculating employees does not apply consistently across industries. Some industries such as the salon industry rely much more heavily on part-time employees than do many other industries. We attract many single mothers who come to our industry for the flexible schedules. Therefore, we have many temporary and part-time employees.

In the application of an employee-based size standard, the SBA currently calculates the number of employees of a business concern as the average number of employees employed for each pay period over the firm's latest 12 months and includes the employees of all affiliates.

In addition, no distinction is made between full-time, part-time, and temporary employees with part-time and temporary employees counted the same as full-time.

The salon industry would be particularly impacted by this system as the average number of hours worked by salon industry employees in a typical week is significantly less than most other nonmanufacturing

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1 industries.

2 According to the Bureau of Labor Statistics,
3 nonsupervisory employees in the salon industry worked an
4 average of 26.4 hours per week in 2004, which is well
5 below the average of 30.7 hours worked by their
6 counterparts in the overall retail sector and 33.7 hours
7 worked in the overall private sector.

8 This means that compared to the vast majority
9 of other industries, a larger number of employees are
10 needed in the labor-intensive salon industry to generate
11 a small amount of sales.

12 It's not uncommon to have over 100 employees,
13 on a different myriad of examples, and generate less
14 than 2 or 3 million for a salon. It's less than
15 3 million significantly.

16 As a result, it takes many more salon employees
17 to generate an annual sales volume that would be
18 considered small in most other industries.

19 If the goal of the SBA is to make size
20 standards as simple and easy to use as possible, I
21 recommend that a receipts-based size standard is the
22 appropriate approach for the salon industry.

23 For small businesses such as salons that have a
24 high proportion of part-time employees, it is much more
25 difficult to track the number of employees than it is to

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1 produce documentation of total annual sales and
2 receipts.

3 The SBA also requested comments on alternative
4 approaches of calculating the employment size of a
5 business concern such as on a full-time equivalent
6 basis. If the goal is to simplify size standards from
7 the perspective of the business community, then
8 establishing a size standard based on full-time
9 employees -- excuse me -- full-time-equivalent employees
10 is definitely not the approach to take.

11 Although it would appear to be more equitable
12 to calculate employee-based size standards on a
13 full-time-equivalent basis rather than by counting
14 full-time, and part-time, and temporary employees
15 equally, it simply would not be feasible in practice.

16 The full-time-equivalent approach would place a
17 tremendous administrative burden on small businesses, in
18 particular businesses that are subject to seasonal
19 fluctuations and those with high proportions of
20 part-time employees such as ours.

21 As I previously mentioned, it would be
22 difficult enough to average the total number of
23 employees, including full-, part-time, and temporary,
24 over a 12-month period. If businesses are also expected
25 to first calculate the number of full-time-equivalent

00124

1 employees for a pay period and then calculate an average
2 of their pay periods over a 12-month period, the
3 administrative burden would be excessive, and many times
4 that administrative burden is resting on the shoulders
5 of the salon owner, who stands behind the chair herself.
6 And it would be excessive.

7 In its Advance Notice of Public Rulemaking, the
8 SBA stated that it remains committed to modifying its
9 size standards in a manner to make them simpler and
10 easier to use.

11 For the reasons mentioned previously, I believe

12 that a conversion to an employee-based size standard
13 would, in fact, make size standards more complicated for
14 the salon industry.

15 Based on the unique characteristics of the
16 salon industry, including the relatively low
17 receipts-to-employee ratio and the high proportion of
18 part-time employees, I believe the current
19 receipts-based size standard is the most appropriate
20 approach for our industry.

21 As such, I respectfully recommend that no
22 changes are made to the size standards for the salon
23 industry, which includes the North American Industry
24 Classification System Codes 812111, 812112, and 812113.

25 Thank you.

00125

1 You've got to remember we keep America
2 beautiful.

3 MR. JACKSON: I need your services.

4 I think I know the answer to this, but this is,
5 as you were talking, kind of a different aspect of the
6 issue about using the number of employees. In your
7 industry and maybe some other industries, if you think
8 about it, you really don't look at the hours worked of
9 your employees, that most individuals are on a
10 commission basis --

11 MS. YAMAGUCHI: Absolutely.

12 MR. JACKSON: And so if SBA were to even
13 consider a full-time-equivalent approach that may work
14 in some other industries like a grocery store or
15 something where you have people checking in at fixed
16 hours, it would appear to be a burden to have to put in
17 some kind of accounting system.

18 Would you agree with that?

19 MS. YAMAGUCHI: Absolutely. You can look at
20 the restaurant association and waiters the wait staff.
21 It's very similar to the way our employees work. And
22 they come for the flexibility. And for us to track the
23 hours is laborious.

24 And so we factor their annual sales, and it's
25 easy to track that. By and large, of the salons that I

00126

1 mentioned, the 60,000 in North America, roughly 75 to 80
2 percent of them are computer based. So it's very easy
3 to track in this format the annual -- so the
4 receipt-based is easy to track. It becomes laborious
5 when it's man-hour based.

6 MR. JACKSON: Thank you very much.

7 MR. ALVARADO: Melissa, I don't know if you
8 have any sense of how many of your members have availed
9 themselves of SBA services, financing and otherwise.

10 And this is true for any of those of you who
11 represent organizations or, again, for you individually.
12 But we'd love to work with you to develop initiatives
13 for your members relative to any one of the programs
14 that I've mentioned or all of them.

15 MS. YAMAGUCHI: We take great advantage of the
16 program. I have -- I don't know the percentage, but I
17 have a huge percentage, I can guesstimate, that are
18 actively involved with the SBA. We had the good fortune
19 at our symposium two years ago to have
20 Melanie Sablehouse come and speak with us and encourage
21 us, really, to take advantage.

22 And we would love to have more information at

23 the hands of our owners so that they could figure out
24 how --

25 MR. ALVARADO: If you can make this man
00127 1 beautiful, there may be a government contract.
2

3 MR. FLORES: Some things are not possible.
4 DELETE.

5 MR. ALVARADO: But he's almost there.

6 MR. KLEIN: Thank you for your time.

7 Kimberley Gill Rimsza.

8 MS. RIMSZA: Good morning. My name is
9 Kimberley Gill Rimsza, R-i-m-s-z-a. And I'm the
10 president of Gill Marketing Company, a division of The
11 Gill Group, Inc. We're NAICS Code 423440 for a
12 wholesaler of durable goods.
13 We're a woman-owned small business. Our family
14 business first incorporated in 1973 with three
15 employees, and we've been growing at a conservative yet
16 steady pace for the past 32 years. We currently have 97
17 employees and expanding. We are a distributor of food
18 service equipment.

19 Gill Marketing is very concerned about the
20 possible change and potential long-term effect on our
21 business if the size standard for nonmanufacturing is
22 changed from 500 to 100 employees.

23 If this change is imposed, it could negatively
24 impact our current and future business opportunities
25 with federal government procurement. We may no longer

00128 1 qualify for future government procurement contracts
2 which we currently hold due to these possible size
3 standard changes and be forced to downsize our operation
4 and terminate valued employees.

5 The proposed size standard change from 500 to
6 100 is extreme and unfair for those companies who have
7 built their business on a platform based on current size
8 standards.

9 We've built our business in good faith that a
10 change of this magnitude would not occur. Companies
11 like ours would or could lose federal procurement that
12 were competitively obtained, thus forcing our business
13 to completely change and perhaps lay off employees or
14 close up altogether.

15 There are many logical reasons why Sector 42
16 currently has a separate size standard for federal
17 procurement, and we're strong supporters of maintaining
18 that current size standard of 500 employees.

19 Federal procurement has different expectations,
20 standards, rules, and overall requirements that are
21 simply more demanding than commercial standards. The
22 infrastructure requires companies to have more resources
23 in the way of employees than other companies in the
24 commercial sector.

25 Further, for a small business such as ourselves
00129 1 to compete with leading federal contractors, small
2 business must be allowed to gain critical mass and a
3 certain size to be able to compete with pricing and be
4 in the competitive range.

5 Lastly, if the size standard is set too low, as
6 being proposed, then once a small business receives a
7 viable small set-aside federal procurement contract and

8 commits the resources, energy, personnel and grows with
9 the contract and then suddenly becomes too large because
10 of that contract or a combination of contracts, it could
11 be detrimental to that small business.

12 At Gill Marketing we're concerned about this.
13 Our contracts address high standards for readiness in
14 case of war and surge requirements. We are prepared to
15 step forward as we have had to these last few years with
16 the war on terrorism and our role in Iraqi Freedom.

17 All of our contracts have grown at a tremendous
18 rate the past several years because of the war efforts,
19 and we've had to add employees, infrastructure, and
20 resources to keep up with our contractual obligations.

21 How many small businesses which currently
22 qualify for federal procurement small business
23 set-asides would lose their qualification status under
24 the potential size standard change and find themselves
25 in the dead or limbo zone -- no longer deemed small yet

00130

1 unable to compete with the larger corporate giants?

2 If the size standards for the nonmanufacturing
3 sector was changed from 500 to 100 for federal
4 procurement, Gill Marketing could very well find itself
5 in the dead zone.

6 In order to service the U.S. military and other
7 federal government agencies, a sufficient infrastructure
8 must be put in place in order that we're able to compete
9 with larger federal government contractors that already
10 have critical mass built into their corporations. It
11 would be different for us to provide the services and
12 meet federal government rules and regulations without a
13 sufficient employee base.

14 One area which takes a great deal of personnel
15 and infrastructure is the federal government reporting
16 requirements, which exceed standard industry business
17 practices, and maintaining and meeting these
18 requirements takes resources, IT capabilities, and
19 employees.

20 In addition, federal government contracting
21 imposes compliance obligations that are not present in
22 the commercial marketplace. These include, for example,
23 the implementation of systems and procedures to comply
24 with proposal disclosure and price reduction monitoring
25 requirements, complying with audit and/or examination of

00131

1 records requirement, and compliance with socioeconomic
2 policies.

3 For larger government contractors, these areas
4 are not the same level of burden because they have many
5 contractors to spread this type of overhead. But for a
6 small contractor, these are resources that add up in the
7 way of cost and personnel commitment.

8 This is one more example why the size standard
9 for small business should not be a different standard
10 for federal procurement than for commercial procurement.

11 In addition, we also have a very real concern
12 if the size standard was reduced from 500 to 100 in that
13 our GSA contract and our Air Force Nonappropriated
14 contracts allow manufacturers to receive direct contract
15 awards.

16 The small business size standard for a
17 manufacturer in our industry is 500 employees. Reducing
18 the size standard for the nonmanufacturing sector would

19 greatly and unfairly impact wholesalers, basically
20 cutting out opportunities in favor of a different class
21 of business.

22 Thank you for this opportunity to present our
23 viewpoint. Questions?

24 MR. JACKSON: Thank you. Just a couple of
25 questions.

00132

1 what percent of your business is with the
2 federal government?

3 MS. RIMSZA: Currently approximately 75 percent
4 is federal government.

5 MR. JACKSON: So any change really affects the
6 core business?

7 MS. RIMSZA: It would be a big impact on our
8 corporation.

9 MR. JACKSON: We've heard testimony at today's
10 hearing and other hearings that, especially in wholesale
11 trade, 98 percent of the businesses have 100 or fewer
12 employees.

13 And right now you're about at that level and
14 growing. Once you grow beyond 100, you're in that
15 fortunate 2 percent that's doing extremely well relative
16 to other firms in your industry.

17 When you reach that point, you mentioned that
18 you don't have the infrastructure that you feel you need
19 to perform on federal contracts and compete. At what
20 point would you achieve that?

21 The 500-employee standard, is that the right
22 level, or is that too high? Too low?

23 MS. RIMSZA: In our opinion, the 500 employees
24 is the right level. And there were some comments made
25 earlier about the bundling of contracts, of federal

00133

1 government contracts, and the size and magnitude of some
2 of these contracts that are now currently being issued.

3 We're seeing more than ever, with these larger
4 contracts being issued and the demands that we're having
5 over in Afghanistan and Iraq what the government's
6 expectations are. They're growing daily.

7 And I think for a small business to be able to
8 address those contracts and the expectations that are
9 coming out of those, we have to be able to meet the size
10 standards.

11 MR. JACKSON: When you say "expectations," in
12 terms of how? Delivery of product or providing services
13 associated with --

14 MS. RIMSZA: Actually both. In our business,
15 we're a distributor, but we're a very high service
16 organization. And our contracts address not only the
17 delivery of food service equipment but full life cycle.
18 So they have high expectations for installation,
19 delivery, warranty service, and general expertise in
20 that area.

21 MR. JACKSON: Thank you.

22 MR. KLEIN: Jeff Di Rado.

23 MR. DI RADO: My name is Jeff Di Rado, spelled
24 D-i, space, capital R-a-d-o. I'm here today with
25 Technology or representing Technology Integration Group.

00134

1 And I'll refer to it as TIG since that is a mouthful to
2 reference every time.

3 TIG is a 23-year-old SBA certified

4 minority-owned small business with corporate
5 headquarters in San Diego, California, and with 20
6 offices throughout the country, one of which resides in
7 Los Angeles.

8 TIG has built a successful business model based
9 upon our status as a minority-owned small business under
10 the current SBA guidelines and prides ourselves on an
11 award-winning diversity supplier track record.

12 TIG's efforts are widely recognized by
13 customers and industry partners. In the past five
14 years, TIG has received 14 industry awards associated
15 with our small business and minority-business ownership
16 status.

17 Our president, Bruce Geier, was personally
18 honored to be recognized by the U.S. SBA as the small
19 business person of the year and SBA's administrator
20 award for excellence.

21 TIG is very interested in continuing as an SDB.
22 We're are committed to continuing to mentor our small
23 minority businesses and actively contribute to the
24 community.

25 We thank the SBA for the ability and

00135

1 opportunity to place our concerns on record today as
2 well as at other venues around the country.

3 TIG strongly opposes all aspects of the SBA
4 potentially changing rules to restructure the size
5 standards by head count or revenue. The management and
6 employees of TIG specifically contest the current and
7 vendor-recommended revisions of the nonmanufacturer size
8 standard from 500 employees.

9 Our company and many other companies like ours
10 could be devastated by the immediate loss of our small
11 business status. My personal division would be impacted
12 directly, as it would financially the personnel that I'm
13 responsible for. And that basically is all of our field
14 personnel, which comprises upwards of 200 individuals.

15 This impact would not be limited to TIG alone
16 but would also adversely impact our business partners
17 and our vendors, which are comprised of both small and
18 large businesses across the United States.

19 So we're not a standalone entity. We
20 incorporate in business partners and vendors and have
21 put together what we consider complex information
22 technology solutions for our clients on the federal,
23 state, local, and education basis. So they would be
24 affected as well.

25 We believe the rules should not be changed or

00136

1 modified. We believe the SBA should concentrate on
2 federal entities' utilization of small business under
3 the existing standards and focus on the correct
4 designation of vendors as a small business.

5 A significant portion of our business is
6 providing quality information technology products and
7 services to the federal government.

8 Additionally, TIG is a small diversity supplier
9 to many state, local, and education customers as well as
10 two large federal prime contractors. Over 70 percent of
11 our overall business is at risk depending upon what
12 changes inevitably are made.

13 TIG is one of the tens of thousands of
14 companies that could lose their small business status

15 depending upon what modifications are made. We do not
16 consider changes to be net neutral but believe that the
17 harm wrought by rule changes will seriously impede the
18 U.S. economy at a time when economic growth and job
19 creation provided by small businesses are critical to
20 the country's welfare and security.

21 Our specific concerns on the potential rule
22 changes are: The SBA has not made a compelling case for
23 the need to change the existing rules.

24 The SBA has failed to provide any supporting
25 documentation to justify its belief that the size

00137

1 standards are complicated and need to be changed.

2 Any change to the nonmanufacturer size standard
3 from 500 employees is a pure net loss. Firms will cease
4 to qualify for federal small business procurement
5 programs.

6 Current small business contracts of any size
7 will go to large businesses such as IBM Global Services,
8 EDS, Lockheed Martin, General Dynamics -- people we
9 routinely have to compete against.

10 Companies with fewer than 100 employees do not
11 have the bandwidth or financial resources to manage the
12 larger contracts. So existing rules should remain
13 intact. What that means is that we do have the ability
14 to serve as the prime. We have enough size and
15 infrastructure.

16 Rule changes encourage companies to find other
17 means to accomplish their tasks other than hiring new
18 employees. In many cases companies will implement
19 immediate layoffs in order to meet the new size
20 standards.

21 Competition benefits both the federal
22 government and the American taxpayers. Rule changes
23 will limit competition by drastically reducing the pool
24 of businesses eligible to compete for federal
25 procurement dollars.

00138

1 If the desire is to reduce the number of
2 classifications from 37 to 10, no rule change is the
3 most acceptable solution to the small business
4 community. If the SBA should continue to consider
5 changing the size standards and/or basing size on
6 revenue, it is apparent that more classifications are
7 actually required rather than less.

8 As an example, a small professional services
9 company may have five employees and generate \$5 million
10 in revenue as opposed to a firm with 280 employees
11 recognizing \$230 million in revenue. Are both small
12 businesses?

13 When you consider that the smaller firm is
14 capable of realizing profits of 20 to 50 percent and a
15 larger firm which provides hardware and software with
16 some supporting professional services may have only 6 to
17 20 percent profit, which is the firm that truly requires
18 assistance of a small business certification? Only the
19 smaller one in size or both?

20 Simple business rules state that it does not
21 matter what you take in but rather what you get to keep.
22 And every firm survives by making a profit sufficient to
23 provide day-to-day survival and future growth.

24 In the best interest of the government
25 procurement, preserving our company and the livelihood

00139

1 of our 274 employees and their families and the welfare
2 of other small business owners and their employees, we
3 urge the SBA to choose the "no rule change" option and
4 immediately withdraw efforts to change the rule.

5 Thank you very much for your time.

6 MR. KLEIN: You said you have 274 employees
7 currently?

8 MR. DI RADO: Currently, yes.

9 MR. KLEIN: How competition-wise can you
10 compete with those greater than 500?

11 MR. DI RADO: We can compete successfully at
12 this level with those greater than 500 right now with
13 this small business designation. It's really the
14 linchpin for us to be able to compete appropriately.

15 We can handle large contracts as a prime. We
16 have one multiple award with the Department of Defense
17 and Department of Energy. So we can do it.

18 MR. KLEIN: Under set-asides, you said?

19 MR. DI RADO: That is correct.

20 MR. KLEIN: Now, how about the firms less than
21 100, can they compete against your size of firms?

22 MR. DI RADO: I think that they would be under
23 duress to do so financially and from an infrastructure
24 standpoint. We are also a services and solution
25 company. We have to employ and keep on bench many

00140

1 technical personnel to go out and be able to not only
2 sell the product but also be able to implement service,
3 support, and continue on a project basis a lot of the
4 technology that we supply.

5 MR. JACKSON: A follow up question to John. In
6 talking about the smaller companies with less than 100
7 employees, again we've heard testimony about
8 recommending the size standard for folks that are
9 nonmanufacturers to be a higher than that.

10 One of the concerns is how competitive are the
11 smaller businesses, especially those with a handful of
12 employees, 20, 30 employees, in competing against the
13 more successful small businesses.

14 I'm not going to ask you a question on the size
15 standard per se but rather a concept we did float in the
16 advance notice on tiering.

17 Given that -- or assuming that the smaller
18 companies, way under 100 employees, are less competitive
19 against the larger small businesses, would you look
20 favorably or unfavorably to some type of tiering that
21 broke out opportunities for some of those smaller
22 businesses, or do you think that is an added
23 complication that may not be necessary?

24 MR. DI RADO: Yeah, I would like the latter
25 that it's an added complication. It might not be

00141

1 necessary.

2 Just to let you know, we do partner routinely
3 with smaller businesses under 100-employee level. We
4 help support them, and they could subcontract us or
5 vice versa. That happens probably more on the state,
6 local, and education environment.

7 As a matter of fact, we're involved in
8 opportunities right now where we are partnering directly
9 with very small firms.

10 In the federal space, we're just big enough to

11 handle those opportunities solely as a prime, and we are
12 just small enough to still qualify, you know, as an SDB
13 under SBA guidelines.

14 And that's why, if people like us end up
15 getting thrown out or getting cut off, the only people
16 that are going to be able to handle larger contracts
17 really are those IBM Global Services and Lockheed
18 Martins and EDS. And I don't think that's what anybody
19 wants.

20 MR. KLEIN: So the result really would be fewer
21 set-asides? Is that what you're thinking?

22 MR. DI RADO: Yes, correct.

23 MR. KLEIN: Thank you.

24 Stephanie McMackin.

25 MS. MC MACKIN: My name is Stephanie McMackin,

00142

1 M-c-M-a-c-k-i-n. I'm the vice president of human
2 resources and risk management for Graphic Press, Inc.
3 We are a commercial printer, and -- basically we're a
4 commercial printer. We print very high-end items.

5 And what I'd like to talk about today is not a
6 change to the size standards other than the way you
7 count employees. We fall under NAICS Code 323110. And
8 so our size standard is 500 employees and under.

9 We don't have a problem with that at all.
10 We're about 250 right now. But like other companies, we
11 would like to grow. And we have another distinction
12 too. With our company, we are somewhat seasonal in that
13 there are times when we really beef up.

14 For instance, right now we are working 24/7.
15 We have three shifts. And on any given day we can use
16 between 60 and 75 temporary employees in our bindery.
17 And if we do that for any length of time and if we do
18 grow in our regular employees and then add our
19 temporaries onto that, at some point that will kick us
20 out of the small business size.

21 We're concerned about that because we do a lot
22 of business with very large Fortune 500 companies who
23 set aside a certain amount of money for dealing with
24 small business.

25 And also, what I forgot to mention is we are a

00143

1 minority-owned company as well. So many times we get
2 our foot in the door as being a minority-owned company,
3 and then they always like to know that we do qualify as
4 a small company.

5 So we are concerned with the fact that you
6 count temporary employees in our count when, in essence,
7 they're really not our employees. We don't pay any
8 benefits for them. We don't really count them into
9 anything that we do for our regular employees.

10 And I would hope that you would take into
11 consideration that perhaps they should be treated as
12 vendors or contractors of some type rather than added in
13 to the employee count.

14 Thank you very much. That's all I have to say.

15 MR. KLEIN: We've heard people talking about
16 full-time equivalent. Would that help at all if we went
17 to that standard versus the current standard?

18 MS. MC MACKIN: I don't think it would. I
19 think it would still kick us over at any point in time.

20 MR. KLEIN: Seasonal work that just comes in
21 sporadically. How does that work? Weeks? Months?

22 MS. MC MACKIN: Months. Let me explain that
23 45 percent of our business is with car books. We do car
24 books for all the major car companies -- Ford, Chrysler,
25 Mercedes, all of that. So we're starting to go into

00144

1 that season now, and we'll be working 24/7 for probably
2 another four, five months.
3 We do a lot of annual reports as well. And of
4 course, that's in the beginning of the year.
5 What we're trying to do now -- our goal is to
6 fill in the slower seasons with more business that is
7 non-car book, non-annual reports. And if we do that and
8 if we do grow and continue to use the same number of
9 temporary employees, that will kick us out of the size
10 standard for our industry.

11 MR. JACKSON: Again, on the temporary
12 employees, those are on your payroll or --

13 MS. MC MACKIN: No, they're strictly --

14 MR. JACKSON: How are they structured?

15 MS. MC MACKIN: We get them through a temporary
16 service called Matrix. We work them on a regular basis.
17 They staff all of our shifts for us in our bindery,
18 primarily our bindery. In very few other departments do
19 we use them.

20 MR. JACKSON: Thank you.

21 MS. MC MACKIN: You're welcome.

22 MR. KLEIN: Nick Smith.

23 MR. SMITH: Can't say "good morning" anymore.

24 I'm Nick Smith, N-i-c-k, S-m-i-t-h. That ought
25 to keep it simple. Our company name is Small Business

00145

1 Consulting Agency. We provide consulting services to
2 other small businesses in assisting them in getting
3 government contracts and working with government
4 agencies.

5 Let me first say I don't envy you guys your
6 job. You have one tough one to crack here, and it's not
7 a simple solution.

8 I would like to speak specifically on the size
9 standards. From all of our clients, when we work with
10 our clients, we drill in them the fact that size
11 standards are important.

12 They've got to maintain their control over
13 their size, watch their growth, and be careful on what
14 kind of contracts that they can take so that they don't
15 grow too rapidly and not have the rest of the support
16 coming along behind it. Most companies fail because
17 they grow too fast and not because of their getting
18 standard growth.

19 Our recommendation is to essentially leave the
20 standards alone. We think the business as employment
21 size is correct for those standards it's applied to, and
22 receipt standards are correct in those areas. They may
23 need some tweaking as industries change, but they're
24 essentially the right concept to go with.

25 We don't like the idea of just taking an

00146

1 arbitrary number of 100 or 10 or 20 or 500 employees and
2 saying that's good for the whole world because there's
3 too much variety in the companies that we work with
4 where we see that they would step in and out of this
5 small business standard.

6 We also want to see that most of the standards

7 that are already multitiered -- or many of them are
8 multitiered already. We have a number of clients who
9 are, depending on what product they're producing, fall
10 into two different standards, even under the same NAICS
11 code.

12 That becomes a problem for them only when the
13 agency doesn't understand the NAICS code has multiple
14 choices because they don't look at the bottom of the
15 NAICS code list.

16 Essentially, that's all I've got to say.

17 MR. JACKSON: I have a question along those
18 lines.

19 In the clients that you do work with, do you
20 find that when they are in situations that they may be
21 small for some NAICS codes or not for others or that
22 they're facing a different set of competitors on certain
23 types of contracts than another, that it leads to
24 complications, or do you think that is not really a
25 serious issue that we need to be concerned about?

00147

1 MR. SMITH: It's like anything else. The
2 better they understand how the code system works, the
3 better they communicate with the buyer and the agency.
4 It becomes a nonproblem.

5 The biggest problem we have is that frequently
6 the agency doesn't understand the codes, or they use the
7 wrong codes to apply to a particular job. We find that
8 more than anything else.

9 MR. JACKSON: Any suggestions on how to improve
10 on that?

11 MR. SMITH: We're a training company. We could
12 teach them all.

13 MR. JACKSON: I'll get your card.

14 MR. ALVARADO: Real quick. You mentioned the
15 idea of measured growth, and that's always an important
16 concept to keep in mind.

17 When you teach firms this, when you counsel
18 them about these concepts -- and there's certainly
19 nothing wrong with it. Somebody might say that's kind
20 of gaming the system, but again, it's quite permissible
21 and appropriate.

22 But does the concept come as a surprise or
23 something new that firms haven't thought of as they are
24 planning their growth and developing their business
25 plan?

00148

1 MR. SMITH: Yes, it does. It becomes very
2 shocking to them, and particularly to the 8(a)'s because
3 they have a third feature they must look at, which is
4 their personal net worth. They have to adjust their
5 company and maintain their control over their company
6 and their personal net worth at the same time. That's
7 kind of a shock.

8 They think, "well, I've got this wonderful big
9 company making lots of money. I could take it all."
10 But they're outside of the 250,000. So yes, it is a
11 shock to the companies that we work with particularly in
12 understanding that measured growth is a better way to
13 go.

14 MR. KLEIN: Thank you.

15 MR. THACHER: Good afternoon. Thank you for
16 the opportunity to speak here. I'm Scott Thacher, CEO
17 and founder of Orphagen Pharmaceuticals. I had a nice

18 long train ride up this morning, which gave me a chance
19 to rewrite my testimony, I'll be sure to send it to you
20 after I'm done.

21 I would like to speak to the SBIR eligibility
22 issue. We've received four grants worth 1.1 million
23 from the National Institutes of Health, or NIH, over the
24 last two years.

25 We have four full-time employees and two

00149

1 part-time. Without this funding, the company would not
2 exist in anything like its present form.

3 I'm here because I'm concerned about the
4 implications of relaxing size standards for SBIR
5 eligibility. At this stage of our development, there
6 are no funding sources that compare with SBIR grants in
7 terms of accessibility and scale.

8 Professional investors that we've talked to and
9 formal advisors and board members have all emphasized
10 this point to me over and over. The message is: Get
11 the program on the move with SBIR funding because
12 angels, VC investors are not ready for what you have.

13 I've been writing SBIR grants for the last
14 three-and-a-half years. Interest and competition for
15 these seems to be at an all-time high, and pay lines are
16 getting tighter.

17 Scientific reviewers are tougher. They're
18 demanding more than we ever expected to go from phase 1
19 studies to phase 2. So under the current regime,
20 there's nothing easy about getting these grants at our
21 stage, and many entrepreneurs that I know of have
22 dropped out.

23 Relaxation of size standards obviously would
24 invite competition from much better funded companies
25 with projects farther along.

00150

1 I would like to divert from the text and just
2 say that there's a lot of good research that goes on
3 outside of SBIR-funded companies. But I understand the
4 purpose of that to be to help companies that have very
5 little other alternative resources for R and D, and
6 that's generally not true of VC-backed firms.

7 So I'm concerned that with expanded eligibility
8 we would not be able to continue or, if we were starting
9 again, not be able to start in the first place.

10 Within the life sciences, our area is
11 early-stage drug discovery. This is a long pipeline.
12 But what we do, generally speaking, is too applied for
13 academia and too preliminary for the established
14 pharmaceutical industry.

15 In our case, SBIR funding for highly risky
16 projects has proven vital. If we're competing with
17 larger, better-funded firms for projects farther along
18 with more preliminary data, I think in the short and
19 long term that we would lose.

20 However, our business model is to file patent
21 applications, carry out proof of principle studies that
22 make us an excellent candidate for VC investment, for
23 partnership with a major pharmaceutical company.

24 We're looking at major areas such as HIV/AIDS,
25 Crohn's disease, metabolic diseases, diabetes, sleep

00151

1 disorders, and cancer. So we're very supportive of the
2 VC industry. It does a terrific job, but we don't want

3 to compete with them.

4 Our funding has attracted
5 scientist-entrepreneurs such as myself who don't fit
6 neatly into academia or industry and find, as I did,
7 that proof of principle studies were not favored, and I
8 needed to go outside to do them.

9 I left a director-level position as a scientist
10 and manager at Allergan, which is a mid-sized
11 pharmaceutical company here in Southern California,
12 before starting Orphagen.

13 Coming with me today was Bob Schultz, a member
14 of our board of directors, who not able to make it. Bob
15 has a success story with SBIR funding with two STTRs,
16 who developed cancer therapy which he then took into a
17 company called "Fabril." "Fabril" has gone public
18 recently and raised \$100 million and has 175 employees,
19 a great example that we would like to follow.

20 So I support the current rules concerning
21 VCC-backed involvement. I would like the greatest
22 clarity possible. I know from talking to many scientist
23 colleagues who have applied in VC-backed funds for SBIR
24 funding that there is resentment and lack of
25 understanding of those.

00152

1 But if those standard have changed, I think
2 small businesses like us will suffer seriously. Thank
3 you very much.

4 MR. KLEIN: We've heard from several people
5 that not allowing the VCC funding eligibility would hurt
6 research in general.

7 Is that something that you can comment on?

8 MR. THACHER: Well, it's a balance. VC-backed
9 firms do good research. It was pointed out earlier,
10 however, they're funding more and more heavily
11 later-stage projects on the D side, the development
12 side, rather than research side.

13 So clearly, there's good research that could be
14 done at VCC firms, but there is great research that's
15 done at Pfizer, Eli Lilly, and the major pharmaceutical
16 companies. The VCC firms generally have equipment --
17 VCC-backed firms have equipment and financial backing
18 that's very significant to have. And an expanded
19 research program is more similar to a major
20 pharmaceutical company.

21 So I think it's an issue of competitive
22 disadvantage and that the funding puts the VC-backed
23 firm in another league.

24 I think also you understand our concept of the
25 model is to bring the technology to a point where it

00153

1 deserves or can attract VC funding for the tens or
2 hundreds of million dollars for product development.

3 MR. KLEIN: At that point if you did get the
4 backing or were eligible for an SBIR award, that would
5 be something that's a logical growth or --

6 MR. THACHER: That is a logical -- I'd love
7 that bargain, to be able to be in the position to
8 compete for SBIR grants. We don't know if we can get to
9 that stage. So we need accessibility now. Later on
10 it's not meaningful.

11 And I've talked about this issue to many people
12 in San Diego, and they say, "Of course, we understand
13 intuitively that VC-backed firms have a lot of money,

14 and you have very little. And it doesn't make sense for
15 you to be competing with them."

16 MR. KLEIN: Thank you very much.

17 MR. THACHER: Thank you.

18 MR. KLEIN: Sharon Merino.

19 MS. MERINO: Hello. My name is Sharon Merino.
20 That's S-h-a-r-o-n, M-e-r-i-n-o. And I'd like to start
21 by thanking you for allowing me to testify.

22 My company is Small Business Consulting Agency.
23 It was founded over 14 years ago. We were founded
24 specifically to assist small businesses in being
25 educated to the 8(a) program, to getting on the 8(a)

00154

1 program, and learning the rules and regulations so that
2 they can compete for contracts within the 8(a) program.

3 As my associate mentioned earlier, one of the
4 biggest problems that we find is that these small
5 businesses get into this program, and they have no idea
6 about the rules and regulations associated with it.

7 We believe that the small business size
8 standards should remain the same with the 500 for the
9 employees and then taking each industry, as you are, for
10 the receipts.

11 However, I think there needs to be a lot more
12 training on rules and regulations because a lot of these
13 small businesses that come into the federal arena are
14 used to dealing in the commercial market. They have no
15 idea when you quote a code or reference a FAR what
16 you're talking about.

17 And to give an example, when you come to the
18 NAICS codes as far as the small business, not knowing
19 which one to use and what the dollar amount related to
20 that NAICS code is and as well as the buyer.

21 For example, you could say that you're going to
22 go out and do dredging or you're to put a tunnel down
23 here. That could fall under special trades. It could
24 fall under general construction.

25 But special trades is \$12 million. So

00155

1 depending on what I'm doing, I could go under the
2 general construction, I would be at \$28.5 million. It
3 all depends on what's called out into the RFP, how the
4 buyer interprets what he's calling out.

5 And unfortunately, the small-business people do
6 not have any training from the SBA so that they learn
7 how to interpret some of these rules and regulations.

8 And we have learned over the years -- and we're
9 a national firm -- we've learned over the years that
10 people have a tendency to come to us and say "the law
11 says." This has nothing to do with the law. Everything
12 that you're doing is rules and regulations.

13 I think there needs to be more training
14 involved with, okay, now that you're in the program,
15 this is what you need to know as far as rules and
16 regulations and how to operate your business.

17 One last note: Because of the fact that the
18 industry is changing so diversely, i.e., technology, 14
19 years ago, 20 years ago, we saw the computer as a
20 massive thing in the corner. Today, luckily, we all
21 have one on our desk.

22 So with that, the industry has changed. You
23 may want to look at the receipts-based, tweak it a
24 little bit. But other than that, I'd say leave it

25 alone.

00156

1 Any comments?

2 MR. JACKSON: Basically, you don't find the
3 system too overly complicated. But it's mainly access
4 to understanding the current requirements that would be
5 more of what SBA should be focused on as opposed to
6 trying to make the system simpler in some way.

7 MS. MERINO: I don't think you're going to make
8 it simpler. And the reason I don't think that is
9 because, first of all, you're very complex. That's just
10 the way you guys are. Okay. And in saying that, some
11 of these people have figured out this much. If you take
12 "this much" away, they're all back to the ground zero.
13 Okay.

14 what I've found -- and you probably aren't
15 going to like this -- but what I've found is this client
16 will call me up and say, "Sharon, I'm this close to
17 hitting my 6 million mark. How can I stay in the 8(a)
18 program?"

19 well, as we mentioned earlier, we teach people
20 how to stay in the program, how to make sure that
21 they're not going to exceed their gross receipts and
22 they're going to not exceed personal net worth. Our
23 goal is to get them out of the program in nine years,
24 become as successful as they are, but stay under the
25 personal net worth so they can stay in the SDB program.

00157

1 with saying that, what we find is the people
2 that have that little bit of knowledge know how to come
3 in and say, "Well, I'm no longer an engineer even though
4 it says that on my license. Now I'm in construction.
5 So I've moved from this position to this position."

6 I'm not saying they're all doing it just to
7 circumvent the program, but they're doing it because
8 sometimes the client, the federal government, has
9 changed their industry. It happens.

10 So these are things we have to keep in mind.
11 You look at a primary SIC code. Most of these people
12 can't give you a primary. They do too many of these
13 little things. I know you want to know that primary is
14 where they make their most money, but sometimes there's
15 not one.

16 So what they do is they try to -- they try to
17 take the rules and -- I don't want to use the word
18 "manipulate" -- but put them into their favor. And at
19 the same time, you have a buyer that does the same
20 thing.

21 So these are all my concerns. Other than the
22 fact I think the size standards should stay the same;
23 other than, as we mentioned before, a little tweaking
24 because there are some industries that have just
25 outgrown those standards, the dollar receipts, I mean.

00158

1 MR. KLEIN: Thank you.

2 MR. ALVARADO: Just for the record, let me add
3 that knowing Sharon, as we have known her for many
4 years, when she says there isn't training provided, we
5 know she's not talking about this office. But we accept
6 that more can be done in this field.

7 And all I would say, though, is that -- and
8 apropos to Nick's point in a bit of a discussion that I
9 was engaging in with him, and that is what some people

would see as good planning, others would see as gaming, and then further down the road, somebody would see it as an attempt to not be in accordance with the spirit if not the letter of the law.

So at some point the whole idea of planning and being judicious in working the system properly is perceived -- and we know it -- by other people as to what are they trying to do. They're not really in accordance with what these programs are for.

MS. MERINO: Well, I hate to say it, but I think one of the biggest disservices that the SBA has done -- and I don't mean this office. Out of all the offices we've worked with, we like this office a lot. Glendale is our favorite.

But the thing is that other offices have a tendency, if they don't know the answer, they say "no"

00159

rather than say, "well, let's explore it. Let's see how we can work with it."

The other thing with that is saying it's because of whom you are, you cannot be perceived as giving additional treatment or preferential treatment to someone else. So you can't say, you know, "when you get to the web page, go here, go here, and go there, and you might find what you need." And that's sometimes what they need. They need hand-holding.

If you are entrepreneur enough and you're driven enough, you're going to find out all the rules and how to play the game. And the reason is because when you find the buyer -- might be brand new, might be old school; don't know -- but when you find the buyer that says, "This is the way it works," you'd better be able to pull out that CFR, the guidelines, and say, "Oh, the way I read it is this way."

There's a lot of money that's being put on the street in contracts that never goes out to bid. And a lot of these people are under the perception, "I get 8(a) certified. I'm just going to get these contracts. I don't have to work for them. They're just going to come to me."

That's the way that it's been told in the marketing phrasing. They don't actually say it, but

00160

it's awfully implied, "If you are 8(a) certified, I could give you a contract." Not necessarily true.

And there are three people last year who graduated out of the 8(a) program without receiving a contract. Not good. Not good. There's got to be more education.

MR. ALVARADO: Sadly, that statistic is replicated all across the country. And I think that's one of the big challenges, and has always been, for the 8(a) program.

And in addition, there's no question that we should all -- as bureaucrats, we like to pride ourselves in this office -- and whether we do a good job on a daily basis, we come back the next day to do an even better job or attempt to.

And that is to be creative and to work within the existing -- I always say we've got the box that really lays out the parameters of the regulations, and there's nothing wrong with going to the edges of the box even as opposed to saying, "well, we've never really

21 gone to the edge. We're always comfortable in the
22 middle."

23 So I think we do challenge ourselves. And I
24 think people like you and others here in the room
25 challenge us to do a better job of that.

00161

1 MS. MERINO: Thank you.

2 MR. KLEIN: Ben Tseng.

3 MR. TSENG: Hello. I'm Ben Tseng, and that's
4 spelled T-s-e-n-g. And I'm here to represent Maxim
5 Pharmaceuticals where I'm the VP of research.

6 And I'm here to address the interpretation of
7 the -- for the SBIR interpretation of the individual
8 ownership rules here.

9 We are a public biotech company, and public
10 biotech companies provide a valuable resource for
11 innovative research similar to the venture cap
12 companies.

13 We are also constantly involved in raising
14 sufficient funds to support the research and development
15 objectives of the company. SBIR funding is important to
16 small public companies to provide the funding for novel
17 ideas that may not be in the company's direct mission
18 but are innovative and address a significant unmet need.

19 In our particular phase, we have had experience
20 on both the private side and also now as a public
21 entity. As a private VC-funded entity, we used SBIR
22 funds to complement some investigational areas, and
23 those include novel therapeutics for cancer and some
24 side effects for cancer therapy.

25 These were funded as being phased fund grants.

00162

1 In the case of the novel cancer therapeutic, it
2 progressed into a phase 2 program. The drug candidates
3 that resulted from the prior SBIR funding, which is now
4 being progressed with clinical studies for early next
5 year, may provide a new class of cancer therapeutics.

6 This progression, however, required some
7 nurturing which was provided by the SBIR grant to bring
8 it to a stage where the early issues were finally
9 addressed.

10 The situation has not changed now that we are a
11 public company in that we are still small in personnel
12 with less than 40 people and limited financial
13 resources. But we still have novel ideas for potential
14 programs that are outside the main focus of the company
15 but of significance such as the example for the
16 biodefense area.

17 We have demonstrated in collaboration with
18 others using our compounds the ability of this compound
19 to offer protection against anthrax -- animal death
20 caused by anthrax or radiation exposure.

21 These are particular areas of interest in
22 biodefense, and a major funding source for such early
23 work is through the SBIR funding mechanism, but which is
24 now no longer available to us due to recent program
25 interpretations.

00163

1 We feel that the interpretation of 51 percent
2 by a natural person for the U.S. for a permanent
3 resident is really restrictive due to the nature of the
4 public investment community being made up largely of
5 institutional investors, particularly in the biotech

6 area.

7 This provides a high hurdle for every public
8 company for the percentage of qualified individual
9 ownership required. Consequently, the present
10 interpretation of the funding guidelines eliminates some
11 of the best solutions for research and excludes small
12 companies such as Maxim Pharmaceuticals who would be
13 considered small by anyone's standard. And Maxim is
14 typical of the majority of public biotechs in America.

15 We feel that the interpretation of individual
16 ownership is and will continue to be detrimental by
17 having those promising innovations not be able to
18 compete for funding.

19 And this, of course, has frustrated scientists
20 in that innovative ideas that we and others have are not
21 allowed the opportunity to compete for funding. And we
22 respectively, hopefully request that the interpretation
23 be changed to allow for consideration of institutional
24 and also VC ownership.

25 Thank you.

00164

1 MR. JACKSON: When you talk about publicly
2 owned, you mean by VCs or stock --

3 MR. TSENG: Publicly traded companies.

4 MR. JACKSON: Are the people that are the
5 owners -- the ownership of that stock, is that by
6 individuals or by companies?

7 MR. TSENG: Just to give you an example, there
8 are institutional ownerships; that is, they could be
9 retirement funds, could be mutual funds that own parts
10 of the company -- that own stock in the company. But
11 there are also a lot of individuals that own it.

12 What happens is that if you restrict it --
13 let's say, commonly it's about 30 to 40 percent is
14 institutional ownership. If you restrict out that
15 number, then the number of individuals, the natural
16 people, who have to own stock, the percentage goes up
17 substantially because you've taken out the pool of
18 institutional ownership.

19 So as an example, if you have a thousand shares
20 and you require 51 percent ownership by individuals, you
21 need 510 shares owned by individuals. If the ownership
22 by institutions represents about 40 percent, then that
23 means you have to have 510 individuals own it out of the
24 remaining 600, which is extremely high for people of
25 U.S. citizenship and permanent residence. And sometimes

00165

1 it's difficult to establish that number.

2 MR. JACKSON: Under our rule that we published
3 last December, technically a publicly traded company can
4 show that individual ownership by the individual shares
5 and by individuals that could qualify, although I have
6 to admit in some situations that we're aware of, it's
7 very difficult.

8 I don't have an answer for you right now other
9 than to say we're aware of that type of situation, and I
10 can't say if there's going to be any policy change
11 there. But I certainly want to convey that the issue
12 has come up several times to the agency, and we're aware
13 of it, and we may be looking into that a lot closer in
14 the future.

15 MR. TSENG: Right. Because I'm sure you're
16 aware that most stock that's owned by individuals is

17 held in brokerage houses.

18 MR. JACKSON: Exactly, yeah.

19 MR. TSENG: So we have no idea what the
20 situation is.

21 MR. JACKSON: Exactly. And again, I can't
22 divulge much information on this other than yes, that
23 it's absolutely correct, and that's one reason we may
24 have to look into that issue further to be fair to your
25 company and others that, if you can't identify that

00166

1 ownership, then how can we try to achieve the objectives
2 of our requirements by doing it in a way that is
3 reasonable for companies to be able to comply with.

4 It a tough challenge, but I wanted to make you
5 aware that yes, that certainly is an issue or a matter
6 that I think the agency needs to look at a lot more
7 deeply before we conclude any review on this whole issue
8 of SBIR eligibility.

9 MR. TSENG: Okay. Thank you very much.

10 MR. JACKSON: Thank you.

11 MR. KLEIN: John Krikorian.

12 MR. KRIKORIAN: I'm John Krikorian. That's
13 spelled k-r-i-k-o-r-i-a-n. I'm a publisher, a
14 consultant, and president of Business Life magazine,
15 Senior Living magazine, and also Krikorian Marketing
16 Group.

17 First of all, I want to thank the local office
18 here. Alberto and his team have been very open. I
19 don't know how the other offices are, but they've been
20 very, very open to small businesses in this area, L.A.
21 County and his districts. It's always been a pleasure
22 dealing with them.

23 15 years ago we started our Business Life
24 magazine here in Glendale, California. And from that,
25 Senior Living magazine came along by a need from people

00167

1 asking us in this community. There is a large growth of
2 baby boomers.

3 Next came Krikorian Marketing Group. My
4 heritage is Armenian. Folks from Armenia came here in
5 the 1920s from the genocide.

6 And one of the things I want to talk about --
7 two things -- one person only this morning mentioned
8 about entrepreneurship. In May it was small business
9 month. We had a special event here in Glendale.
10 Entrepreneurship is the backbone of America. Small
11 business is the backbone of America.

12 In this area, L.A. County, small business has
13 been exploding, not at the rate of 500 when they open
14 the door but at the rate of one, two, three, four family
15 businesses, home-based businesses.

16 So I firmly believe that change is necessary in
17 the size of business, not change for the sake of change
18 but change for making a difference for small business,
19 to give them the advantage.

20 I heard this morning that small businesses with
21 under 100 people are stressed out because they can't
22 meet the demand for grants and business itself. That's
23 too bad. They should be able to meet it, and they
24 should have the advantage.

25 I heard this morning people say there's a lot

00168

1 of duress for small business if they're under 500.

2 There's are too many businesses growing here with
3 opportunities that are small, small businesses.

4 We have five employees. We contract out with
5 the state, and we contract out with the county for small
6 business.

7 Another thing I would like to talk about too is
8 outreach, community outreach. As Alberto knows, here in
9 Glendale there's a large settlement of Armenians,
10 probably the largest number of Armenians in the U.S.A.
11 outside of Armenia itself.

12 We have two contracts going, one in effect
13 right now that's going to be coming out the end of July
14 on bioterrorism. It's a major contract that came out.
15 The federal came to the state, came down to the county.

16 We would like to see a wider net to be more
17 inclusive of the makeup of America today. The contract
18 we have is educating the Armenian community, the Arabic
19 community, the Iranian community, and the Russian
20 community on homeland security, what to do on
21 bioterrorism.

22 We just completed a contract on secondhand
23 smoke that again came out from the federal to the state
24 to the county.

25 So what I'm asking is down the road -- the

00169

1 census 2000, we handled the contract for that back in
2 the year 2000 for those four communities -- to be
3 prepared to reach out to all of America, to count
4 everybody in America when that census in 2010 comes out.

5 It was a major challenge for us to educate --
6 Alberto knows -- he's here in this office -- that there
7 are a large number of Armenians, there's a large number
8 of Iranians, there's a large number of Arabic folks, not
9 only in this area but in Dearborn and other pockets of
10 the United States.

11 They need to be educated in their language.
12 And in Glendale, for example, the Armenian has 11
13 newspapers that are in the Armenian language -- 11
14 newspaper -- dailies, weeklies. And they're the
15 predominant paper.

16 We're going to educate these people on small
17 business issues. We dealt with this with Alberto. They
18 have to be reached in their language as the Hispanics
19 are, as the Asian communities are, and so on.

20 So, yes, I feel that you have to change the
21 laws on size. I feel that you have to scatter your net
22 out to the more inclusive to different ethnic groups in
23 this country, non-English-speaking groups, and also to
24 simplify the methods of doing business.

25 The county we work with very close. The state

00170

1 we work with closer. With the federal government, it's
2 been a major challenge for us. Maybe we are too small
3 to do business with the U.S.A. but that's about it.

4 MR. KLEIN: Thank you.

5 In terms of size, do you have specific
6 recommendations on your industry? Are you happy with
7 our --

8 MR. KRIKORIAN: Well, my industry is basically
9 we're consultants, professional services, and we're
10 smaller -- as I mentioned, we have five. And we compete
11 against firms that are hundreds of folks.

12 So I think there has to be some sort of level

13 of incentive for small companies to be subcontractors.
14 On some of our contracts that we have, we are
15 subcontractors. The primary contractor should send out
16 a net to say, "We need help in this area. Let's reach
17 Krikorian Marketing or whoever."

18 You know, Sharon does a job helping out with
19 different companies that, I think, are ten, five, a
20 hundred to be competitive in certain fields. Public
21 relations, marketing, communications is our Krikorian
22 Marketing Group.

23 MR. ALVARADO: John, just to be clear, I'm a
24 bureaucrat. So I don't understand things often.

25 MR. KRIKORIAN: You understand perfectly well.

00171

1 MR. ALVARADO: In general, I don't -- that's
2 why I read your magazine. I'm working on my Armenian.
3 I speak it with a Mexican accent.

4 In general, you don't favor increasing the
5 standards? You --

6 MR. KRIKORIAN: I want them decreased to a
7 smaller size.

8 MR. ALVARADO: Okay.

9 MR. KRIKORIAN: Now, we don't compete against
10 firms with 500 employees when we're five. They have the
11 resources. They have the CPAs. They have the attorneys
12 that can sit down for hours and fill out the forms, and
13 we don't.

14 We just went through a whole circle jerk on
15 HAVA, which is the voting initiative. We spent hours
16 overtime, brought in people to submit our proposal.
17 Went down to the wire, and then it ended up in the
18 wastebasket in Sacramento.

19 There was no recourse. Could we have sued the
20 state? We thought about it. AND it would have gone to
21 the federal government. For us, it was a major, major
22 cost, and then it just got -- the person is not in
23 office any longer. It was a big fiasco

24 MR. KLEIN: Thank you.

25 Helen Anderson.

00172

1 MS. ANDERSON: I'm Helen Anderson. I'm CEO of
2 Rayvern Lighting. I'm president of Anderson Associates,
3 a small business consulting company. And I sit on a
4 number of advocacy boards, one being Small Business
5 California.

6 And I thank you very much for coming here and
7 having this hearing. Last November the issue arose on
8 small business, and there was an outcry for the input
9 from small business.

10 And I appreciate that you have come all the way
11 from Washington to hear us in mainstream America and at
12 the grassroots level. It's certainly a different
13 perspective than if you're having hearings solely in
14 Washington.

15 I don't want to be redundant about a number of
16 the speakers here, but it will at least put a face to a
17 name to Mr. Jackson.

18 An association that I had belonged to -- I had
19 been on the board of trustees -- National Small Business
20 Association. I chaired their procurement committee had
21 served on that until last December.

22 And a letter was submitted to you on a number
23 of the issues that people talked about on our position

24 list. So I will pass that on to you.
25 I want to reemphasize how vital it is to keep

00173

1 the current standards. For small business to be
2 competing in the arena with these larger businesses is
3 almost impossible because of their infrastructure and
4 their wherewithal.

5 It is so critical for our communities that
6 small business has support. We're the infrastructure.
7 In L.A. County alone, 51 percent of the businesses are
8 small business. They contribute to the economy. They
9 create jobs. And as the speaker before me said, they're
10 part of the community infrastructure.

11 Big corporate America does not have that same
12 sense. In the primes with the DOD, Boeing is moving its
13 corporate office to Chicago. They pick up and move.
14 They lay off people. And small business is much more
15 critical in their community and their contribution. So
16 I think it's vital to keep small business sizes as they
17 are.

18 I question if the numbers are increased, how
19 this will impact the 8(a) program. With the greater
20 sophistication of larger businesses, with the
21 infrastructure, will they gobble up the money in the
22 8(a) program? Because access to capital is so critical
23 to the infrastructure of small business to do not only
24 business with the government but to continue to grow.

25 What will the impact be if we increase the size
00174

1 to what the President's executive order is for
2 unbundling contracts? If the size standard increases to
3 a thousand, then, of course, the pool is larger, but
4 what happens when you whittle down to the smaller-size
5 business that wants to compete on an RFP on a federal
6 contract? You're really in a position of noncompete
7 then.

8 I speak of this as a wholesaler. I have ten
9 employees. I work in commercial and industrial
10 arenas -- schools, municipalities. But on the federal
11 level, as the pendulum swings between bundling and
12 unbundling, I'm often competing on a bundled contract
13 with my manufacturer. So that's a no win.

14 As the President signed the executive order to
15 unbundle, there has not been enough fulfillment of this
16 standard and utilization of small business even at the
17 present level. I think we need to work harder on that.

18 I can share with you very briefly the impact of
19 a small business owner in terms of pricing, but there's
20 very little time left. But I would like to refer you to
21 the California case -- antitrust case on pricing, how it
22 impacts the small business person to compete. And if
23 you get the sizes larger, we won't even be there.

24 It is "Chroma" Lighting vs. Osram Sylvania,
25 Case No. 94555-81, and that will really be very

00175

1 enlightening in terms of how the oligopolies control the
2 marketplace.

3 And I thank you very much for having these
4 hearings in California and want to add to the record how
5 wonderful Mr. Alberto Alvarado is. He is the jokemaster
6 of Southern California, but also a very, very able
7 leader of the SBA here.

8 MR. ALVARADO: You're very kind. Thank you.

9 MR. KLEIN: Ms. Anderson, one question for you.
10 You're in the wholesale trade category, and
11 with that testimony similar to yours, some have
12 advocated not more than a hundred employees size
13 standard.

14 But we've heard from a couple of companies that
15 are in between 100 employees and 500 that have made the
16 comment that they did not feel that some of the smaller
17 distributors could fulfill the requirements of
18 government contracts for whatever reasons. I don't need
19 to reiterate their points.

20 What's your response to that? How do you look
21 at your competitive -- or your ability to perform on
22 government contracts as a relatively smaller small
23 business?

24 MS. ANDERSON: We can compete on federal,
25 state, county level contracting. I enjoy a master

00176

1 agreement with the county and competed with, you might
2 say, the big boys.

3 Today the biggest challenge for me, or probably
4 for any small business in wholesale distribution, is the
5 cost of a barrel of oil. Just a few years ago it was
6 \$29.00. It is now \$60.00 a barrel. And government
7 contracting requires full freight allowed.

8 So you're getting it from the manufacturer. In
9 the past they would pay that to go out. But now we have
10 to incur all that cost. And all of the costs attendant
11 to that are going up. So we can't really pass that on
12 to the end customer.

13 But the cost of energy is going to be critical
14 to any small business in distribution, more critical
15 than the size of your work force.

16 MR. KLEIN: Thank you.

17 Sharon Edlin.

18 MS. EDLIN: I'm Sharon Edlin, spelled
19 E-d-l-i-n. I'm the CEO of the EDS, Inc. We're about 17
20 years old. We're not under the -- we're a regular small
21 business.

22 Two points I want to address, one has to do
23 with the -- forgive me, I can't remember the NAICS
24 conversion code, but under the old SIC, 8711 except
25 weapons system.

00177

1 Our firm is purely an IT services firm. Our
2 customers are 100 percent Department of Defense. And
3 the reason I decided to speak today is because that
4 conversation seems to have been missing. I want to
5 address the point of what is under 8711.

6 In fact, five years ago a very large firm was
7 900 million. Today a very large firm is 5 billion.
8 Five years ago a small firm may have been 200,000. Now
9 a small firm, meaning an emerging firm, brand new, is
10 already starting at 500,000 to a million.

11 What causes this is because we're purely
12 services now. In the IT business arena, as you can
13 pretty well know reading the papers, the cost of labor
14 has gone up over the last five years 25 to 30 percent.

15 When you go to buy or to employ a programmer or
16 software developer out of college, their wages are
17 somewhere around \$65,000 a year. Five years ago they
18 were 35,000. Our SIC code is still 23 million.

19 Today our average labor cost, especially in the

high-tech world -- and we're dealing with many of your national security agency type functions -- is an average of \$100,000 a year per employee.

So if you just do the math, you can see that 23 million is not the same threshold that it was five years ago. So that's an important point.

So I'm an advocate of either increasing that revenue base to accommodate an industry that is rapidly changing or moving to the 500-employee mark. Now, I'm only addressing 8711 because I know there are other industries that don't see it that way.

And that's the reason why I'm speaking today, is because you're looking at the high-tech industry where you need to have -- you still need to have small business, but everything is relative. A small business for us -- in the services business, as you can see, \$500,000 is five employees. So that's an important point.

The second thing I would like to talk about or point I'd like to make is an emerging business. Our firm, like I said, is 17 years old. I know what it was like to be an emerging business, and I know it's difficult to -- when you start out, to look at your business's future, to make decisions for your business's future when you're still struggling to try to get your systems in place, try to maintain those 20 employees that you tried so hard to bring on board.

The most important thing, I think, for any business owner is to look to the future. I'm not sure how the other industries work, but I do know in the 8711 industry, as an emerging business, there's no

stratification. We literally started with five employees, won one federal contract, and immediately started competing with Northrop Grumman.

So I am a proponent of stratification in that particular SIC as well. I would like to see some kind of an emerging business threshold; maybe 100 employees would be it.

500 employees might very well fit that mold for 8711 because 500 employees is not going to be that much larger than your -- it would probably be about 40 million. If you look at it, relatively speaking, we're under 5 billion.

So my question really is: When you think of these things even outside of the 8711, think about what you're defining as large business. Okay.

MR. JACKSON: Just for the record, 8711 is now 541331. A few NAICS codes I have memorized.

So to help address some of the concerns of the smaller small businesses, some type of tiering might be a consideration that we should look at?

MS. EDLIN: I would think so. Now, I'm only speaking from experience. You know, one of the things that occurred to us when we hit 10 million is all of the sudden we recognized -- and I'm talking about growth process again -- that we had to get cost accounting

systems in place, we had a lot of infrastructure that we had to basically support that we didn't have to before.

And it puts you in a whole different ball game, so to speak. While you're trying to take care of

5 infrastructure and then all of a sudden bidding
6 contracts, which also requires capital, it's pretty
7 tough, and that's just from experience.

8 You know, a lot of times what happens is when
9 you're 100 employees, you think, "Oh, my gosh, I can't
10 compete with the big business. They have 200." But
11 that isn't even a big business.

12 MR. JACKSON: Again, we get testimony from both
13 sides, and tiering, again, is one area that we have been
14 interested in comments for that reason. The smaller and
15 larger small businesses have different needs and
16 requirements.

17 MS. EDLIN: I think at least in the IT
18 industry, that would be beneficial. I know Mr. Alvarado
19 was talking about assisting in that growth process even
20 for 8(a) programs. And this is one way that you can
21 assist them, is get them by phases into industries so
22 they can compete on their own.

23 MR. KLEIN: Thank you.

24 Robert Zimmerman.

25 MR. ZIMMERMAN: My name is Bob Zimmerman.

00181

1 That's B-o-b -- I'm dyslexic, but my mom gave me that
2 name so I could spell it -- Zimmerman,
3 Z-i-m-m-e-r-m-a-n. I'm the CEO, president, janitor for
4 Veteran Government Services.

5 Haven't heard anybody so far talk about
6 veterans. I'm a service-disabled veteran and own a
7 small business located in Escondido, California, down
8 close to San Diego.

9 Mr. Alvarado, I'm sorry you didn't pay me 20
10 bucks to say something nice about you.

11 MR. ALVARADO: Please don't let that limit you,
12 now.

13 MR. ZIMMERMAN: You know, I've heard about
14 beltway bandits and bureaucrats. Mr. Jackson, I've
15 talked to you three times, and I just want to tell you
16 that, first of all, you look a little more distinguished
17 than I thought about when I talked to you on the phone.
18 But you always gave me your time.

19 There was one particular time -- and you may
20 recall it -- when I gave you my comments. There was
21 about a 30-minute conversation on the size
22 determination, and you really educated me. And I just
23 want to thank you publicly because you take that bar of
24 what a bureaucrat in D.C. is all about, and I really
25 appreciate the opportunity to talk to you.

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1 And I think, as a former marine, I should be
2 able to stand away from the mike and make you hear my
3 comments.

4 You know, sir, I gave 30 years to God, country,
5 and the corps. And I find jobs for people that have
6 come back, and unfortunately I can't find jobs for those
7 that don't. But I can for the widows.

8 And I don't want the SBA to stand in the way of
9 finding jobs for what my job is, and that's to find jobs
10 for people that need them. That's what I do.

11 And there's NAICS codes that are just out of
12 whack. Okay. 561210, 541210, 561320, and 541410. And
13 those are right off the top of my head. In my prepared
14 remarks, I was told that I wasn't going to be able to
15 say anything because I didn't submit it earlier. So I'm

16 just talking off the top of my head.
17 So I'm going to continue those -- but
18 facilities, temp services, and human resources
19 professional consulting. And then there's some more.
20 There's employment agency NAICS codes, and they range
21 from 6 million to 30 million.
22 And of course, for small business owners trying
23 to compete on federal contracts, it's real hard to take
24 a widow with two kids out of Camp Pendleton, and I can't
25 get her a job because I can only compete on this one job
00183
1 that's got a \$6 million limitation. So I'm not eligible
2 to compete for that.
3 So what I should do is have something
4 simplified. I know Napoleon conquered Europe because he
5 gave his plans to a corporal, and if the corporal
6 couldn't understand it, he changed his plans. Now,
7 there's a lesson, and the lesson is: Just make it
8 simple.
9 And in the people business -- and I heard some
10 people talk earlier about the people business -- it's
11 not hard to figure out. And I really believe that
12 you're on the right track if you think that 500
13 people -- I mean it's been a standard that's been used,
14 and I've heard comments both ways. But that sounds like
15 a good number, 500 people.
16 And in the temp business -- and I don't like
17 the word "temp business" because in the contracting
18 business or in the federal business a temp only says 240
19 days or 120.
20 But according to the government reformed
21 management act, you can have contract employees who can
22 go for the length of the contract. And that's what we
23 in the real world are trying to compete for.
24 So I'm looking for simplified, standardized 500
25 employees throughout those NAICS codes that we're trying
00184
1 to provide as real world industry jobs for people that
2 need them.
3 You know, that was going to be pretty much the
4 extent of my comments. Except that there's an executive
5 order for SDVOSBs, the service disabled veteran owned
6 small businesses. Nobody else showed up, I guess, that
7 would fall under that category of the executive order of
8 3 percent.
9 And according to your site, in 2002 there's
10 only been 0.17 percent -- and that was actually half
11 from the year before -- of federal contracts given to
12 service-disabled veterans.
13 Now, I've been through two wars and got beat up
14 pretty bad. And I stand at the gate of Camp Pendleton
15 or go down Point Loma to the sub base, to 32nd Street to
16 the navy, I go to Miramar, and I go to the recruit depot
17 trying to get these veterans jobs. And they need them.
18 So do the widows.
19 I'm responsible for hiring, firing, screening,
20 testing, and placing contract employees with the federal
21 government. That's my job. I'm responsible for my own
22 profit and loss. I have to go out and market and
23 advertise and write up all the RFPs and 120 pages for
24 those solicitations.
25 I have to provide the benefits for my
00185

1 employees. Also, I outsource my own payroll, and I
2 outsource my factoring to, you know, get my accounts
3 receivable.

4 And you know, that's the same as I heard -- and
5 this wasn't -- I'm not a franchisee. I don't want to be
6 a franchisee. I've never been a franchisee. I heard
7 small businesses stand up today and say they did the
8 same thing I did, they had the same responsibilities.
9 The only thing is they've got some, you know, corporate
10 that does the outsourcing of their AR. But they're
11 doing the same thing I do.

12 And the point being, is that in doing some of
13 the major contracts as a small business, I can't get
14 them because I don't have a national presence. But if I
15 could use another agency like the franchisees that do
16 the same thing I do, I could compete nationally with
17 some of the -- you know, the number one staffing company
18 that just happens not to be a U.S.-owned company but
19 takes all of our taxpayers' money -- that's an editorial
20 comment, by the way.

21 That's the extent of my comments. Thank you,
22 sir

23 MR. JACKSON: Thank you, Mr. Zimmerman. A
24 couple of quick things.

25 You mentioned that you operate in a number of
00186

1 NAICS codes, that those standards need to be revised.
2 It sounds like in terms of simplification, more common
3 size standards would be what you think would be a move
4 in the right direction.

5 Would that be a fair assumption?

6 MR. ZIMMERMAN: That is beyond fair. If you
7 made that, you'd be my hero.

8 MR. JACKSON: Well, I can't do that at the
9 moment, but I might be your hero with other information,
10 and I know you probably know Bill Elmore from our office
11 of --

12 MR. ZIMMERMAN: Oh, yeah, I get his e-mails all
13 the time.

14 MR. JACKSON: Good. Bill is working very hard
15 for veterans, believe me. I know him well, and one of
16 the most committed people we have in the agency.

17 MR. ZIMMERMAN: Absolutely. Great man.

18 MR. JACKSON: We also just filled the position
19 in the government contracting area for our office of
20 veterans business government contracting. I forget the
21 exact title of that office. But Theresa Artis -- she's
22 former military, recently retired from the Air Force
23 Reserves.

24 But we're beginning a significant outreach
25 effort to implement such a program for service-disabled
00187

1 vets. You're going to hear more and more about that
2 throughout the years. So there are a lot of things the
3 agency is doing to help our veterans. So I just wanted
4 to relay that to you while we have the opportunity.

5 Thank you.

6 MR. ZIMMERMAN: Again, thank you for spending
7 time with me.

8 MR. KLEIN: I think at this point we've had
9 everyone who has appeared on the list in the back.

10 Is there anyone else present who would like to
11 speak who has not been called at this point?

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Okay. I want to thank you very much for
(The proceeding adjourned at 1:08 p.m.)